Supreme Court, U.S.
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No. 01-

IN THE

Supreme Court of the United States

A.D. BEDELL WHOLESALE COMPANY, INC., TRIANGLE CANDY & TOBACCO CO., on behalf of themselves and all others similarly situated,

Petitioners,

v.

PHILIP MORRIS INCORPORATED, R.J. REYNOLDS TOBACCO COMPANY, INC., BROWN AND WILLIAMSON TOBACCO CORP.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

The four largest cigarette manufacturers, having a 98% share of the nationwide market, entered into a settlement agreement with 46 States to resolve lawsuits brought by the States against them. The settlement agreement contains provisions that substantially penalize any firm entering into that agreement including smaller competitors, who later signed on to the agreement for exceeding their agreed upon output. Two cigarette wholesalers brought this antitrust action on behalf of all direct buying wholesalers claiming that the output restriction is illegal *per se* under the antitrust laws. The court below held that the manufacturers' acts in furtherance of the output restrictions were immune from antitrust scrutiny under the *Noerr-Pennington* doctrine even though they did not qualify as state action under this Court's decision in *Parker v. Brown*:

1. Does the *Noerr-Pennington* doctrine immunize an output cartel controlling an entire interstate market because the provisions creating it were inserted into a settlement agreement with a group of states?

2. Does the *Noerr-Pennington* doctrine apply to an output cartel's post-petitioning anticompetitive conduct that has no antitrust immunity under state action doctrine?

3. Do the Supremacy Clause, the Commerce Clause and the Compact Clause preclude a group of States from using the *Noerr-Pennington* doctrine to immunize the operation of an interstate output cartel?

LIST OF ALL PARTIES IN THE PROCEEDING AND CORPORATE DISCLOSURE STATEMENT

All parties to the proceeding are identified by name in the caption. Neither of the petitioners, A.D. Bedell Wholesale Company, Inc., nor Triangle Candy & Tobacco Co., are subsidiaries or affiliated with any other corporation, and no publicly-held company owns 10% or more of the stock of either of these petitioners. This is a class action brought on behalf of all direct buying wholesalers of cigarettes from the respondents. Prior to its dismissal, however, no certification was made.

TABLE OF CONTENTS

	Page
Questions Presented	i
List of all Parties in the Proceeding and Corporate Disclosure Statement	ii
Table of Contents	iii
Table of Cited Authorities	v
Table of Appendices	xi
Opinions Below	1
Statement of Jurisdiction	1
Constitutional Provisions and Statutes Involved	1
Statement of the Case	3
A. Preliminary Statement	3
B. The Facts	5
1. The Failed Congressionally Sanctioned National Settlement	5
2. The Majors and the States Strike a Deal Without Congress	8
3. The Provisions in the MSA Setting Up the Output Cartel	9

Contents

	Page
Reasons for Granting the Writ	14
1. The Court Below Has Decided an Important Question of Federal Law in a Way that Conflicts with Relevant Decisions of this Court	14
2. The Court Below Incorrectly Applied the *Noerr-Pennington* Doctrine	20
3. The Court Below Has Decided an Important Question of Federal Law That Has Not Been, But Should Be, Definitively Settled by this Court: Whether *Noerr-Pennington* Immunity Should Be Extended To Settlement Agreements With States	21
4. The Court Should Address the Issue of Whether the Supremacy, Commerce and Compact Clauses Preclude *Noerr-Pennington* Immunization of the Interstate Output Cartel	24
5. The Court Below Improperly Concluded that The Constitutional Objections To Antitrust Immunity Defenses Were Not Raised in the District Court	28
Conclusion	30

TABLE OF CITED AUTHORITIES

Page

Cases:

Allied Tube & Conduit Corp. v. Indian Head, Inc., 486 U.S. 492 (1988) 15, 20, 21

Andrx Pharm., Inc. v. Biovail Corp., 256 F.3d 799 (D.C. Cir. 2001) 21

Bacchus Imports, Ltd. v. Dias, 468 U.S. 263 (1984) 12, 25

Baldwin v. G.A.F. Seelig, Inc., 294 U.S. 511 (1935) 26

Bayou Fleet, Inc. v. Alexander, 234 F.3d 852 (5th Cir. 2000), *cert. denied*, 121 S. Ct. 1228 (2001) .. 29

Broadcast Music, Inc. v. CBS, Inc., 441 U.S. 1 (1979) 17, 21, 22, 23

Brown-Forman Distillers Corp. v. New York State Liquor Auth., 476 U.S. 573 (1986) 25

California Motor Transport Co. v. Trucking Unlimited, 404 U.S. 508 (1972) 23

California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc., 445 U.S. 97 (1980) 17

Campbell v. Chicago, 823 F.2d 1182 (7th Cir. 1987) 23, 24

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Cited Authorities

Page

Dennis v. Higgins, 498 U.S. 439 (1991) 12

Eastern R.R. Presidents Conference v. Noerr Motor Freight, Inc., 365 U.S. 127 (1961) ..... *passim*

Edgar v. MITE Corp., 457 U.S. 624 (1982) 27

Forces Action Project LLC v. California, No. C 99-0607, 2000 WL 20977 (N.D. Cal. Jan. 5, 2000) 19

Forces Action Project LLC v. California, No. 00-15280, 2001 WL 923124 (9th Cir. Aug. 15, 2001) 19

FTC v. Superior Court Trial Lawyers Ass'n, 493 U.S. 411 (1990) 15, 16

FTC v. Ticor Title Ins. Co., 504 U.S. 621 (1992) .. 18

Hartford-Empire Co. v. United States, 323 U.S. 386, *clarified*, 324 U.S. 570 (1945) 21

Healy v. Beer Institute, Inc., 491 U.S. 324 (1989) 25, 27

Hise v. Philip Morris, 46 F. Supp. 2d 1201 (N.D. Okla. 1999), *aff'd in an opinion not for publication*, 208 F.3d 226 (10th Cir. 2000), *cert. denied*, 531 U.S. 959 (2000) 18, 19

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Cited Authorities

Page

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North Carolina Elec. Membership Corp. v. Carolina Power & Light Co., 666 F.2d 50 (4th Cir. 1981) 29

Northern Securities Co. v. United States, 193 U.S. 197 (1904) 30

Otter Tail Power Co. v. United States, 410 U.S. 366 (1973) 17

Parker v. Brown, 317 U.S. 341 (1943) .... i, 3, 12, 17, 19

Patrick v. Burget, 486 U.S. 94 (1988) 16

Philip Morris v. Blumenthal, 123 F.3d 103 (2d Cir. 1997) 22

Premium Tobacco Stores, Inc. v. Fisher, 51 F. Supp. 2d 1099 (D. Colo. 1999) 19

Primetime 24 Joint Venture v. Nat'l Broadcasting Co., Inc., 219 F.3d 92 (2d Cir. 2000) 21

PTI, Inc. v. Philip Morris Inc., 100 F. Supp. 2d 1179 (C.D. Cal. 2000) 19

Cited Authorities

Page

Quill Corp. v. North Dakota, 504 U.S. 298 (1992) 12, 25

Rice v. Norman Williams Co., 458 U.S. 654 (1982) 25, 30

Schwegmann Bros. v. Calvert Distillers Corp., 341 U.S. 384 (1951) 18, 25, 30

Southern Motor Carriers Rate Conf. v. United States, 471 U.S. 48 (1985) 18

Star Scientific, Inc. v. Carter, Civ. Act. No. IP 01-0838, 2001 WL 1112673 (S.D. Ind. Aug. 20, 2001) 12

Star Scientific, Inc. v. Earley, No. 3:00CV835 (E.D. Va., Mar. 26, 2001) 12

United Mine Workers v. Pennington, 381 U.S. 657 (1965) ..... *passim*

United States v. Singer Mfg. Co., 374 U.S. 174 (1963) 21

United States Steel Corp. v. Multistate Tax Comm'n, 434 U.S. 452 (1978) 27, 28

Virginia v. Tennessee, 148 U.S. 503 (1893) 27

Cited Authorities

Page

United States Constitution:

Art. I, Section 8 ..... 1, 5, 29

Art. I, Section 10 ..... 2, 5, 27, 28, 29

Art. VI, Clause 2 ..... 1, 29

Statutes:

15 U.S.C. § 1 ..... 1, 2, 25, 29

15 U.S.C. § 2 2

15 U.S.C. § 15 3

15 U.S.C. § 16 3

26 U.S.C. § 468B 11

28 U.S.C. § 1254(1) 1

28 U.S.C. § 1331 3

42 U.S.C. § 1983 *et seq.* 19

Page

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D.J. Tice, "States on Big Tobacco's Side After Smoke Clears," St. Paul Pioneer Press, Aug. 31, 2001 .. 22

5 CHARLES ALAN WRIGHT & ARTHUR R. MILLER, *FEDERAL PRACTICE & PROCEDURE*, § 1276 (Civ. 2d 1990) 29

TABLE OF APPENDICES

Page

Appendix A — Opinion And Judgment Of The United States Court Of Appeals For The Third Circuit Dated And Filed June 19, 2001 ..... 1a

Appendix B — Opinion And Order Of The United States District Court For The Western District Of Pennsylvania Dated March 22, 2000 ..... 65a

Appendix C — Consented-to Order Of The United States District Court For The Western District Of Pennsylvania Dated April 11, 2000 ..... 87a

Appendix D — Order Of The United States Court Of Appeals For The Third Circuit Denying Petition For Rehearing Dated July 24, 2001 ..... 89a

A.D. Bedell Wholesale Company, Inc. and Triangle Candy & Tobacco Company, on behalf of themselves and all others similarly situated, petition the Court for a writ of certiorari to review the judgment of the United States Court of Appeals for the Third Circuit.

OPINIONS BELOW

The Opinion of the United States Court of Appeals for the Third Circuit is reported at 263 F.3d 239 (3d Cir. 2001) and reprinted at petitioners' appendix (Pet. App.) at 1a-62a. The Opinion of the United States District Court for the Western District of Pennsylvania dismissing the complaint herein and denying petitioners' motion for partial summary judgment on the issue of liability under Section 1 of the Sherman Act, 15 U.S.C. § 1 is published at 104 F. Supp. 2d 501 (W.D. Pa. 2000) and reprinted at Pet. App. at 65a.

STATEMENT OF JURISDICTION

The Court of Appeals entered judgment on June 19, 2001 and denied petitioners' petition for a rehearing and suggestion for a rehearing *en banc* on July 24, 2001. Pet. App. at 88a. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

U.S. Constitution

Art. VI, Clause 2. Supreme Law of Land

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof: and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

Art. I, Section 8. The Congress shall have Power To lay and collect Taxes, Duties, Imports and

Excises, to pay the Debts and provide for the common Defense and general Welfare of the United States; but all Duties, Imposts and Excises shall be uniform throughout the United States.

Clause 3. To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes.

Art. I, Section 10. Clause 3. No State shall, without the Consent of Congress, lay any Duty of Tonnage, keep Troops, or Ships of War in time of Peace, enter into any Agreement or Compact with another State, or with a foreign Power, or engage in War, unless actually invaded, or in such imminent Danger as will not admit of delay.

The Sherman Act

15 U.S.C. § 1. Trusts, etc., in restraint of trade illegal; penalty

Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal. Every person who shall make any contract or engage in any combination or conspiracy hereby declared to be illegal shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding $10,000,000 if a corporation, or, if any other person, $350,000, or by imprisonment not exceeding three years, or by both said punishments, in the discretion of the court.

15 U.S.C. § 2. Monopolizing trade a felony; penalty

Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commence among the several States, or with foreign nations, shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine

not exceeding $10,000,000 if a corporation, or, if any other person, $350,000, or by imprisonment not exceeding three years, or by both said punishments, in the discretion of the court.

STATEMENT OF THE CASE

This is a class action under the antitrust laws brought under 15 U.S.C. §§ 15, 16 and 28 U.S.C. § 1331, giving the federal district courts exclusive jurisdiction of such actions.

A. Preliminary Statement

This case presents an issue of critical importance to the interpretation and application of the federal antitrust laws. The court below decided that a restraint of trade agreed to and implemented by private parties that fails to qualify for state action protection under *Parker v. Brown*, 317 U.S. 341 (1943), is nonetheless immune from antitrust scrutiny under the *Noerr-Pennington*[1] doctrine whenever the private parties request to have the restraint incorporated into a settlement agreement entered into with a group of states.

That decision conflicts with decisions of this Court and recent decisions of the Circuit Courts of Appeal. Indeed, the decision would effectively eviscerate *Parker* if it were allowed to stand. Under the lower court's reasoning, the conduct of private parties and restraints of trade that fail to satisfy the state action doctrine, either because they are not clearly articulated as state policy or closely supervised, are immune from scrutiny whenever the parties lobby or request a state government to agree to the restraint. The lower court failed to recognize, however, that *Noerr-Pennington* does not apply to the subsequent operation of a restraint or its implementation by private parties. Thus, immunity for the subsequent operation of the cartel and the acts of its members must be judged under *Parker, not Noerr-Pennington*; and, as the court below decided,

1. *Eastern R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127 (1961); *United Mine Workers v. Pennington*, 381 U.S. 657 (1965).

the restraint and conduct causing antitrust injury fails to qualify for state action protection.

This case also presents an issue of critical importance to the limits of the encroachment by a group of states upon the powers of the federal government in regulating interstate commerce. It transcends the legality of the cartelization of the industry involved here — the nationwide cigarette market. The cartel was created in an agreement called the Master Settlement Agreement ("MSA") made between the major manufacturers and 46 states to settle claims arising from state expenditures for illnesses associated with smoking.[2] Under the rationale of the lower court's decision (hereafter sometimes referred to as the "Opinion"), such industry-wide cartels can now be created through settlement agreements between a combination of states and the major firms in any industry, the only limitation being an industry concentrated enough to enable such a cartel to work effectively. The gun industry, the oil refining industry (pollution from benzene), and the heavy truck industry (pollution from carbon particulate matter, nitrogen oxide, and damage to state roads) are obvious candidates.

Indeed in the amicus brief submitted by the states to the Third Circuit in this case, they maintained that it is "vital" for the States to "remain free to engage in meaningful settlement negotiations with private parties they sue and to conclude settlement agreements with them." Amicus Brief of Settling States at 4. The cartel validated by the Opinion presents a win-win situation for the cigarette companies on the one hand and the states on the other. It enables the cigarette companies and the states to split annually billions of dollars in supracompetitive revenues generated by the restraints of trade

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2. In addition, six other governmental entities (the District of Columbia, Puerto Rico, the Virgin Islands, American Samoa, Guam and the Northern Mariana Islands) joined the MSA. They, together with the 46 States, are defined in the MSA as the "Settling States". Joint Appendix submitted to the Third Circuit in this case (hereinafter referred to as "JA") at 105 (MSA § II (qq)-(rr)).

embodied in the settlement agreement. The ultimate losers are wholesalers and the millions of consumers of cigarettes.[3]

Moreover, even if settlements made with states were entitled to *Noerr-Pennington* immunity, granting such immunity to the acts implementing cartelization of a nationwide industry encroaches on the enumerated powers of the federal government. It directly interferes with interstate commerce in violation of the Commerce Clause, U.S. Constitution, Art. I, § 8, cl.3 and the Compacts Clause, U.S. Constitution, Art. I, § 10, cl.3.[4]

B. The Facts

The facts are accurately stated in the Opinion and will only be briefly summarized here. The three defendants, together with a fourth cigarette company (the "Majors") had 98% of the nationwide cigarette market in November, 1998. Pet. App. at 4a. At that time, they entered into a multi-state settlement agreement with the Settling States, the so-called Master Settlement Agreement ("MSA"), in which they agreed to make annual multibillion-dollar payments in perpetuity. Pet. App. at 49a-51a; JA 126 (MSA § IX(c)).[5]

1. The Failed Congressionally Sanctioned National Settlement

Starting in the mid-1990's, a number of states filed claims against the Majors seeking to recover health care costs associated with illnesses relating to smoking. The Majors sought to settle these claims by getting most of the states' attorneys general to agree in the Spring of 1997 to seek to obtain congressional enactment of a proposed national legislative settlement. JA 400.

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3. The direct-buying purchasers, mostly wholesalers, the class suing here, are the only parties with standing to seek antitrust damages from the defendants. *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977).

4. As discussed *infra*, p. 28, the Opinion's assertion that the petitioners did not raise the Commerce Clause and Compact Clause arguments in the district court is incorrect.

5. The MSA and the exhibits thereto are also available on the website of the National Association of Attorneys General (hereafter "NAAG"): www.naag.org.

The Majors and the States then presented a proposed national settlement to Congress in June 1997, which provided for the same sort of output cartel subsequently embodied in the MSA. Proposed Tobacco Industry Settlement, June 20, 1997[6]; *see also* Pet. App. at 5a.

The 1997 National Settlement Proposal would have required annual payments which were much larger than those called for in the MSA — about $15 billion per year and aggregating approximately $368 billion over twenty-five years,[7] *id.* at Title VI(B), and were structured so that they would force smokers to pay for all of these costs by means of a pass-through. The FTC estimated the pass-through costs to consumers for funding this settlement at somewhere between 57¢/pack and 99¢/pack over that 25-year period. FTC Report on Competition and the Financial Impact of the Proposed National Tobacco Settlement (JA 497, 540) (September 1997) (hereinafter the "September 1997 FTC Report"). The FTC estimated that the manufacturers could finance the entire proposed $368.5 billion settlement by raising prices during this 25-year span by a *total* of about 60¢/pack.[8] JA 540.

The 1997 National Settlement Proposal would have protected the Majors from any competitive disadvantage versus existing smaller competitors or others, who might thereafter enter the market and use their cost advantage to take market share away from the Majors. It contained the prototype for the restriction on output ultimately embodied in the MSA. It classified as a "Non-Participating Manufacturer" ("NPM"),

6. Available at http://www.cnn.com/us/9705/tobacco/docs/proposal.html (last visited June 18, 2001).

7 By contrast, under the MSA, assuming that efficient policing of the cartel results in the Majors' losing little or no market share to competitors, they will pay to these states about $211 billion over a 25-year period. JA 125-26 (MSA §§ IX(a), (b) and (c)).

8. Even though the MSA annual payments are many fold less than this $15 billion, the Majors have now raised prices by more than 60¢/pack. JA 679-80. That sum was the total aggregate price rises postulated by the FTC needed to fund the $368.5 billion settlement over 25 years.

Proposed National Tobacco Settlement at Title III (C), all cigarette makers except for the four Majors; and provided, for example, that an NPM which captured 2% of the domestic cigarette market would be forced to pay 3% of the $15 billion annual settlement payments ($450 million), rather than having to pay merely 2% of the allocable settlement payment that the Majors would otherwise have to pay for that same market share ($300 million or 2% of $15 billion), *i.e.*, a penalty of $150 million. *Id.* The Majors' aliquot share of the $15 billion settlement would be correspondingly reduced by $450 million. Such a penalty, of course, would have effectively prevented the NPM's from capturing market share through price competition, thereby preserving the output cartel.

The 1997 National Settlement Proposal explicitly provided an additional exemption from the antitrust laws for the Majors. This proposed exemption would have permitted them to "jointly confer, coordinate or act in concert, for this limited purpose [of achieving the goals of the settlement]." *Id.* at Appendix IV (C)(2); *see also* JA 557 (FTC evaluation).

In September 1997, the FTC's formal evaluation of the proposed settlement condemned the proposed output cartel contained in the settlement as a vehicle for generating supracompetitive revenue for the Majors. JA 517, JA 534. In subsequent testimony before Congress in October 1997, FTC Chairman Pitofsky specifically objected to the excessive profits the Majors would make:

> The analysis contained in the FTC Staff Report demonstrates that approximately two-thirds of any additional revenues generated as a result of increased industry coordination will go to the manufacturers as excess profits.[9]

9. This is roughly the same split as the Majors achieved with the MSA. However, the actual price rises already made by the Majors since the MSA was executed in November, 1998, 63¢/pack (exclusive of the 10¢/pack federal excise tax increase on 1/1/00), are much higher than those posited by the FTC. Hence, the Majors are making far more (Cont'd)

Prepared Statement of FTC Chairman Pitofsky before the Subcommittee on Antitrust, Business Rights and Competition, October 29, 1997.[10] He then pointed out that the "antitrust exemption could permit firms to raise cigarette prices beyond the level necessary to satisfy payments under the settlement, resulting in a windfall to the industry." *Id.* As discussed below, this is what the Majors have accomplished through the MSA.

2. The Majors and the States Strike a Deal Without Congress

The FTC's opposition resulted in the scuttling of the 1997 National Settlement Proposal. Pet. App. at 7a. By early 1998, the Majors had settled health care lawsuits with four states, Florida, Mississippi, Texas and Minnesota, totaling about $40 billion in payments to those states over twenty-five years.[11] JA 400. In the Spring of 1998 the Majors restarted the negotiations with the remaining state attorneys general and the private plaintiffs' attorneys with the output cartel still the centerpiece of the proposed negotiations but this time with no antitrust exemption. The deal culminating in the MSA containing the provisions for an output cartel without an antitrust exemption was executed as of November 23, 1998. Pet. App. at 7a; JA 85-247.

The MSA also differed from the earlier proposed national settlement in several significant respects — all of which favored the Majors. First, as noted above, the payments to the states were substantially less, about 60% of what the national settlement would have required, thereby enabling the Majors to retain more of the excess revenue generated by the cartel.

(Cont'd)
supracompetitive profits under the MSA than those projected by the FTC under the failed national settlement.

10. Available at http://www.ftc.gov/os/1997/9710/tobacco.tes.HTM.

11. Those four states are not parties to the MSA, but the Majors can deduct the payments to them from the payments due under the MSA — the so-called Non-Settling States Reduction. JA 102 (MSA § 2(dd)).

See supra p. 6. Second, the tobacco industry would not be regulated by the FDA or required to print additional and stronger health warnings on cigarette packs. Third, the Majors could continue sports promotions of brand labels and cigarette advertising, both in print and at retail stores. In addition, MSA §§ III(c)(2)(i), III(c)(3), III(f), III(i) gave the Majors grandfather rights for brand name sponsorship, giveaways of merchandise and promotions. JA 107-111. Fourth, the private plaintiffs' attorneys assisting the states' attorneys general are now receiving and will continue to receive billions of dollars in fees from the operation of the cartel. JA 163 (MSA § XVII(d)); JA 207-24 (MSA Exh. O); JA 163 (MSA § VII(d)); JA 201-24 (MSA Exh. D).

3. The Provisions in the MSA Setting Up the Output Cartel

The provisions of the MSA setting up the output cartel are described in the Opinion (Pet. App. at 7a-16a and 19a-21a) and will only be briefly summarized here. They consist of an interlocking combination of three provisions: the so-called Renegade Clause, MSA § IX(i), the provision for States' enacting escrow statutes, MSA § IX(d)(2)(B)(D) and (E), and Exhibit T to the MSA (the so-called "Model Statute" discussed in the Opinion (Pet. App. at 12a-15a)), and the NPM Adjustment for Original Participating Manufacturers ("OPM's"), MSA § IX(d)(1), quoted in full and discussed in the Opinion. Pet. App. at 9a-12a.

If a small manufacturer joins the MSA, thereby becoming a "Subsequent Participating Manufacturer" ("SPM") or refuses to join, thereby becoming a "Non-Participating Manufacturer" ("NPM"),[12] any attempt to increase its output is effectively penalized so as to enable the Majors to raise prices to artificially high levels without losing significant market share. If it joins the MSA as an SPM, the small manufacturer is required by the terms of the Renegade Clause to pay substantial penalties for

12. These are defined terms in the JA 102, 106 (MSA §§ II(cc) & (tt)).

exceeding the greater of its 1998 market share or 125% of its 1997 market share. JA 137 (MSA IX(i)(1)). This penalty, approximating about 40% of the wholesale price, net of the penalty, thereby effectively discourages price competition.[13]

On the other hand, if a small manufacturer declines to join the MSA as an SPM, it is subjected to even stiffer penalties as an NPM under the Escrow Statutes. The MSA penalizes the Settling States unless they use their best efforts to enact an Escrow Statute, which must contain the provisions of a "Model Statute." JA 131, 241-45 (MSA Exh. T).[14] These Escrow Statutes constitute the last turn of the screw making this output cartel watertight. In the MSA, the Majors and attorneys general agreed to impose severe penalties by way of reduction of settlement payments on any state that did not enact an Escrow Statute. This so-called NPM Adjustment results in a substantial reduction in annual settlement payments to that particular state. JA 131 (MSA § IX(d)(2)(F)). Not surprisingly, all of the Settling States have now enacted Escrow Statutes. Section IX(d)(2)(E) of the MSA explicitly confesses the anticompetitive purpose of these Escrow Statutes: to establish a means "that effectively and *fully neutralizes the cost disadvantages* that the Participating Manufacturers experience *vis-a-vis* Non-Participating Manufacturers within such Settling State as a result of the provisions of this Agreement." *Id.* at JA 131, emphasis added. To make sure that the States enforce the Escrow Statutes,

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13 *See* Opinion (Pet. App. at 8a-9a). The 1999 penalty was about $1.90 a carton, or nearly 40% of the typical 1999 wholesale price of about $5.00 per carton for discount cigarettes. JA 476-77. For every carton of discount cigarettes an SPM sold in 1999 in excess of its market cap, the SPM had to pay over about 40% of the $5.00 it received. Operating margins, however, were substantially less than 40% (JA 441), thus making the penalty prohibitively expensive and forcing the SPM to raise prices and forego increased sales.

14. The Escrow Statutes also are defined as "Qualifying Statutes" under MSA § IX, thereby entitling the various state attorneys general to use the slush fund to lobby for their enactment and to enforce them.

the NPM Adjustment is triggered with respect to any State that does not "diligently enforce" its Escrow Statute. JA 130 (MSA § IX(d)(2)(B)).

The *in terrorem* effect of the Escrow Statutes on a potential new competitor in the discount end of the market is obvious. They coerce new entrants into paying for the past sins of the Majors by forcing them to pay an allocable share of the MSA payments, even though they have not been accused of and cannot in good faith be assessed for any wrongdoing.

The Escrow Statute penalties, which are roughly the same dollar amount as those imposed upon sales of SPM's in excess of their market cap under the Renegade Clause, are more severe because, unlike the MSA settlement payments, they are treated as fully taxable income, *i.e.*, after-tax dollars. They are non-deductible for income tax purposes because they are not "settlement" payments, 26 U.S.C. § 468B, and remain nominally the property of the NPM's, even though they are paid into a perpetual 25-year revolving fund that must be placed in a bank escrow account. JA 244 (MSA Exh. T); Pet. App. at 14a. At the end of 25 years whatever has not been paid out of the first year's payment is replaced by the penalties accrued in year 26, and so on in perpetuity. JA 244 (MSA Exh. T).[15] Although the Opinion characterizes the escrow payments as "a tax on new tobacco entrants of approximately $.27/pack in the year 2001, rising to $.36/pack by the year 2007" (Pet. App. at 13a-14a), the drafters of the MSA carefully defined these payments so as to avoid their being legally characterized as taxes. Had they been imposed as *de jure* taxes, they would have been facially discriminatory as favoring members of the cartel and thus *per se* violative of

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15. In the event an NPM does not make these escrow fund payments, the attorney general of each state is authorized to sue and assess a civil penalty on the recalcitrant NPM "in an amount not to exceed 5% of the amount improperly held from escrow per day of the violation and in a total amount not to exceed 100% of the original amount improperly withheld from escrow." JA 245 (MSA Exh. T).

the Commerce Clause. *See, e.g., Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 270-72 (1984).[16]

To assure that the reach of the MSA output cartel extended nationwide, stretching into the four non-MSA states, Florida, Mississippi, Texas and Minnesota, the Escrow Statutes have an extraterritorial application. They require an NPM to make escrow payments on its cigarettes sold in Settling States "directly or through a distributor, retailer or similar intermediary." JA 244 (MSA Exh. T). Thus, if an NPM sells to Wholesaler X located in Minnesota, which in turn resells those cigarettes to Retailer Y in Wisconsin, that NPM must make escrow fund payments on the cigarettes sold at retail in Wisconsin. The direct interference with interstate commerce and violation of the NPM's civil rights under the Commerce Clause by enforcing this indirect sale requirement is obvious. *See, e.g., Quill Corp. v. North Dakota*, 504 U.S. 298 (1992); *Dennis v. Higgins*, 498 U.S. 439, 446 (1991).

The result has been nearly total cartelization of the nationwide cigarette industry. This cartelization has enabled the Majors to overcharge wholesalers and ultimately the millions of purchasers of cigarettes throughout the entire country by billions of dollars annually and, unless this petition for certiorari is granted, in perpetuity.

To date, the cartel has satisfied the full expectations of its participants. On November 23, 1998, the day after the MSA

16. The extraterritorial reach of these statutes has been sustained on the precise ground that they are not sales taxes. *Star Scientific, Inc. v. Carter*, Civ. Act. No. IP01-0838, 2001 WL 1112673 (S.D. Ind. Aug. 20, 2001). The constitutionality of these Escrow Statutes was unsuccessfully challenged on grounds other than their being preempted by the Sherman Act and violative of the Commerce Clause by virtue of their constituting a nationwide restraint on interstate commerce illegal under the Sherman Act. *Star Scientific, Inc. v. Earley*, No. 3:00CV835 (E.D. Va., Mar. 26, 2001). That decision is now on appeal to the Fourth Circuit, Appeal No. 1-1502. The lack of antitrust immunity under *Parker v. Brown* found by the court below was not raised by Star in the district court.

became effective, Philip Morris and R.J. Reynolds announced the largest price increase in the 100-year old history of this industry: 45¢/pack. Pet. App. at 15a-16a. B&W, Lorillard and Liggett quickly followed. This colossal price increase was the largest in dollar amount ever taken in the history of American marketing for any product: nearly $11 billion a year, *i.e.*, far more than the 19¢/pack necessary to make the $2.47 billion initial payment, as well as the next $4.5 billion payment which was due on April 15, 2000. JA 125 (MSA § IX(b)) and JA 126-27 (MSA § IX (c)). The 45¢/pack increase was more than double the amount that the Majors needed to fund the settlement. Pet. App. at 14a-16a.

Not content with the billions of supracompetitive revenues generated by this initial $4.50/carton price increase, at the end of August 1999 the Majors announced an additional wholesale price increase of $1.80/carton, generating an additional $1 billion in revenues for the last four months of 1999, none of which was necessary to fund the MSA payments due on April 15, 2001.[17] Then in January 2000, the Majors boosted prices by yet another $1.30/carton, and another $1.00/carton in April 2001. All told, these price hikes increased the cigarette revenues for the Majors nearly $14 billion for the year 2000, over twice as much as the payments required by the MSA.[18]

To summarize, to finance a settlement, the Majors realized as early as 1997 that they needed to have in place an output cartel. In 1997, Congress, at the urging of the FTC, denied them the *de jure* antitrust exemption that they had requested. Undeterred, in 1998 they proceeded to enter into the MSA with

17. The figure for the 1999 figure is derived by extrapolating from the Philip Morris for 1999 10K sales data available at www.sec.gov/Archives/edgar/data/764180/0000912057-00-009516.txt.

18. The $14 billion is computed by multiplying the estimated number of cigarettes to be sold in 2000, 2.15 billion cartons by the three price increases totaling 76¢ minus the 10¢ per pack increase in the federal excise tax effective in January 2000, or $6.60 x 2.15 billion cartons, by assuming that the output cartel enabled the Majors to retain at least a 96% collective market share for the year 2000.

the Settling States whereby those states agreed to bestow upon the Majors' monopoly profits for as long as the cartel set up in the MSA would last. Although the states came to destroy the Majors, they "settled" their healthcare claims by agreeing to collaborate with them to virtually eliminate all future competition and split the supracompetitive revenues generated by this restraint. They proclaimed "victory" over the Majors, but that victory consists of agreeing to take and in fact taking all steps they can to assure that the Majors' sales of cigarettes continues to prosper through the efficient operation of the cartel, thereby exploiting the millions of purchasers of cigarettes and rewarding the bad conduct of the Majors to the tune of billions of dollars. In a final piece of irony, the attorneys general have agreed to award the private plaintiffs' attorneys who assisted them in setting up this cartel with annual fees totaling billions of dollars. JA 162 (MSA § XVII (d)); JA 207-24 (MSA Exh. O).

REASONS FOR GRANTING THE WRIT

1. The Court Below Has Decided an Important Question of Federal Law in a Way that Conflicts with Relevant Decisions of this Court

The court below recognized that the *Noerr-Pennington* doctrine immunizes private parties from antitrust injury related to petitioning activity, *i.e.*, injury that results from the petitioning itself, but went on, however, to immunize injury not caused by the petitioning itself but rather the post-petitioning anticompetitive conduct of private parties. Pet. App. at 24a-32a, 41a. That this is the injury immunized by the lower court is clear from the court's statement that "the anticompetitive injury here resulted from the tobacco companies' conduct after implementation of the [MSA], and not from any further positive action by the States." Pet. App. at 41a.

By so extending the protection of *Noerr-Pennington*, the lower court decision conflicts with several decisions of this Court. The first is *Pennington* itself. *United Mine Workers v. Pennington*, 381 U.S. 657 (1965). That case limited the protection for petitioning activity to the petitioning activity itself.

In *Pennington*, a group of large coal mine operators, together with a union, petitioned the Secretary of Labor and the TVA to set up minimum wages in coal mines supplying the TVA. *Id.* at 660. This Court explicitly denied protection to certain of the resulting anticompetitive restraints implementing that petitioning activity that were directed at driving small mine operators out of business. *Id.* at 663. This Court explained that if "the union became a party to a collusive bidding arrangement designed to drive [plaintiff] and others from the TVA spot market, we think any claim to exemption from antitrust liability would be frivolous at best." *Id.*

In the same vein, this Court's rulings in *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492 (1988) and *FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411 (1990), recognized that restraints of trade, even though closely connected to petitioning activities but undertaken by private parties unsupervised by any governmental body, are not immunized under *Noerr-Pennington*.

Allied Tube held that the adoption by state and local governments of an electrical code for buildings did not immunize the restraints undertaken by the steel tube manufacturers that petitioned to get the code enacted to eliminate a plastic tube manufacturer as a competitor. It stated:

> . . . we hold that at least where, as here, an economically interested party exercises decision-making authority in formulating a product standard for a private association that comprises market participants, that party enjoys no *Noerr* immunity from any antitrust liability flowing from the effect the standard has of its own force in the marketplace.

Id. at 509-10. This holding is particularly apposite here in light of the lower court's conclusion that the States exercise no active supervision of the operations of the cartel. In fact, the lower court pointed out:

> The States here are actively involved in the maintenance of the scheme, but they lack oversight or authority over the tobacco manufacturers' prices and production levels. These decisions are left entirely to the private actors. Nothing in the Multistate Settlement Agreement or its Qualifying Statutes give the States authority to object if the tobacco companies raise their prices. In fact, it appears these increases have already happened. As noted, the Majors have raised their prices sharply and uniformly since the implementation of the Multistate Settlement Agreement according to plaintiffs, by 50% since 1997. *See* Complaint at ¶ 36. These price increases have not been monitored or regulated by the States. The Multistate Settlement Agreement imposes no restrictions on pricing or provisions to temper the effects of the output cartel.

Pet. App. at 56a-57a.

Similarly, in *Trial Lawyers*, the public defenders of the District of Columbia engaged in a concerted refusal to represent indigent defendants in order to pressure the District into raising the hourly rate paid. *Trial Lawyers*, 493 U.S. at 414-19. This Court held that the defendants could be held liable under the Sherman Act for injuries that resulted directly from the boycott, even though the boycott was intended to secure government action. *See also Patrick v. Burget*, 486 U.S. 94, 100-01 (1988).

The illegal acts here dovetail with the Examples II and III posited by 1 PHILIP E. AREEDA & HERBERT HOVENKAMP, *ANTITRUST LAW*, ¶ 229 (2d ed. 2000), as being unprotected by *Noerr*, where they point out:

> The private party is not immune where the operative restraint results from its own private action inadequately supervised by government pursuant to a policy to displace the antitrust laws.

Id. at 519.

The Opinion also conflicts with, and would extend the state action immunity doctrine of *Parker v. Brown* to cover interstate commerce without any limitations. Through the restrictions on the output of the Majors' small competitors, the MSA has displaced competition with an output cartel designed to allow the Majors to raise prices without losing market share. *Parker* holds that anticompetitive actions by the states in their governmental capacities as sovereign regulators are not barred by the antitrust laws. *Parker v. Brown*, 317 U.S. 341, 352 (1943). *Parker* immunity, however, must satisfy several conditions to be effective. One such condition emphasized by *Parker* itself, 317 U.S. at 362-63, is that the restraint must relate to the state's local, intrastate activities. *Id.* at 359-63. Another was expressed in *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980), which held that when private parties purport to act pursuant to state action, the action must be clearly articulated state policy and closely supervised by the state. *Id.* at 105. By immunizing the unsupervised acts done on a nationwide scale by implementing this output cartel, the Opinion read these initial limitations out of existence.

The effect of the Opinion expands the local activity limitation inherent in the state action immunity doctrine beyond its judicially recognized boundaries. The state action doctrine is based on the right of a state to regulate matters of local interest and conduct occurring within its borders. There is no such thing as "interstate action immunity." If that were not the case, every nationwide anticompetitive restraint embodied in a settlement made between a group of competing private firms and a state or group of states would be entitled to antitrust immunity. Such immunity would exist even though the restraint pervasively controls interstate commerce. If federal officials in the executive branch lack the power to grant such dispensation, and they do,[19] it is an anomaly to hold that state officials are imbued with such power, particularly since this Court has ruled that state officials

19. *See Otter Tail Power Co. v. United States*, 410 U.S. 366, 378-79 (1973); *Broadcast Music, Inc. v. CBS, Inc.*, 441 U.S. 1, 13 (1979).

and even state legislatures lack such power. *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621, 631 (1992); *Schwegmann Bros. v. Calvert Distillers Corp.*, 341 U.S. 384 (1951).

The importance of these issues is manifested by the fact that the decision below, in finding that no state action exists with respect to the output cartel, presents an anomaly in the future enforcement of the antitrust laws. For example, the protections of *Noerr-Pennington* extend only to private parties — in this case the Majors; the states have no similar *Noerr-Pennington* protection. Thus, if wholesalers or consumers sue to enjoin the states from enforcing the MSA's output restrictions, the wholesalers and consumers would prevail on any immunity issue as a matter of law, because, as the court below found, the output restraints fail to satisfy the requirements of state action. Pet. App. at 51a-60a. Thus, the effect of the decision below is that a restraint may be enjoined if it fails to qualify for state action protection in a case brought against a state; yet, the same restraint cannot be enjoined when the private parties who agreed to the restraint and act in furtherance of it are sued and claim *Noerr-Pennington* protection on the basis that they asked for the restraint. This Court has made clear that the scrutiny a restraint of trade must receive cannot turn on which parties to the restraint — private entities or states — are sued. *Southern Motor Carriers Rate Conf. v. United States*, 471 U.S. 48, 58 (1985). ("The success of an antitrust action should depend upon the nature of the activity challenged, rather than on the identity of the defendant.") A suit against either should yield the same result.

Further uncertainty and confusion in this area, which again can only be cleared up by this Court's granting this petition, arises from conflicting rulings, albeit at the district court level, with respect to immunization of the output cartel and the MSA under the antitrust laws. These are *Hise v. Philip Morris*, 46 F. Supp. 2d 1201 (N.D. Okla. 1999), *aff'd in an opinion not for publication*, 208 F.3d 226 (10th Cir. 2000), *cert. denied*, 531 U.S. 959 (2000), two other unrelated actions involving gray

goods (*i.e.*, U.S. cigarettes sold for export and imported back into this country), *Premium Tobacco Stores, Inc. v. Fisher*, 51 F. Supp. 2d 1099 (D. Colo. 1999) and *PTI, Inc. v. Philip Morris Inc.*, 100 F. Supp. 2d 1179 (C.D. Cal. 2000),[20] as well as another consumers' class action under 42 U.S.C. § 1983 *et seq.* which in effect challenged the price increases after the MSA as illegal taxes. *Forces Action Project LLC v. California*, No. C 99-0607, 2000 WL 20977 (N.D. Cal. Jan. 5, 2000). The district court in *Forces Action* found absolute immunity under the Eleventh Amendment and did not permit the consumers there to amend their complaint to allege that the MSA contains unreasonable restraints of trade. *Id.* at *2-7. The District Court held that the consumers, as indirect purchasers, did not have standing to seek injunctive relief based on a violation of the antitrust laws. *Id.* The Ninth Circuit, however, reversed and remanded the case to the district court. *Forces Action Project LLC v. California*, No. 00-15280, 2001 WL 923124 (9th Cir. Aug. 15, 2001). Although the Ninth Circuit had been advised of the Third Circuit's ruling on state action immunity, its *per curiam* reversal did not explicitly address the issue, but it did allow the plaintiffs to seek an amendment to plead the antitrust case against these state officials. *Id.* at *1-2.

This Court should resolve these issues by brightening the demarcation line between *Noerr-Pennington* and *Parker*, and reaffirming that *Noerr-Pennington* governs the petitioning, while *Parker* governs the result of the petitioning.

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20. *Hise* was a consumers' class action seeking antitrust treble damages on conclusory and unsubstantiated charge of price fixing. The opinion in *Hise* did not discuss state action immunity because it was the first case involving the MSA and that defense apparently never occurred to the Majors at that time. As to the *Noerr* immunity issue, the Majors responded to plaintiffs' amicus brief by explaining to the Tenth Circuit that the complaint in the instant case was "premised on factual allegations not part of the record [in *Hise*]" and that "the theory that the MSA allegedly involved unlawful output restrictions . . . [was] inapposite [in *Hise*]." JA 662.

1 PHILIP E. AREEDA & HERBERT HOVENKAMP, *ANTITRUST LAW*, ¶ 229 (2d ed. 2000), expresses the correct rule this way:

> As a result, (a) the private party is immune for requesting an anticompetitive statute or government order later found not to have *Parker* immunity; but (b) the private party may not be immune for its actions subsequently undertaken under this nonimmune statutory regime, particularly for its unsupervised anticompetitive conduct.

Id. at 519.

2. The Court Below Incorrectly Applied the *Noerr-Pennington* Doctrine

Although the Opinion correctly ruled that the doctrine of state action does not immunize the illegality of the price increases that the Majors implemented after executing the MSA, it never explains why they are protected under *Noerr-Pennington*. The antitrust injuries sued on herein flow from the Majors' implementing the output cartel and raising prices by $7.60/carton up through January 17, 2000 (Pet. App. at 16a, n.22, 20a-21a) and another $1.00/carton in April 2001. As the Opinion points out, the illegality of these price increases implementing the output cartel cannot be protected under the state action immunity doctrine because the States had no supervision over these price increases, since they "are left entirely to" the Majors. Pet. App. at 55a-56a.

Here, as reveled by the Opinion's own analysis of the antitrust injuries (Pet. App. at 16a-23a), as well as to why state action immunity is unavailable (Pet. App. at 45a-60a), the antitrust harm sustained by plaintiffs results *solely* from private action. The Opinion here conflicts with the rule that where the direct antitrust injury is attributable to acts of the private party, those acts are not immunized under *Noerr-Pennington*. *Pennington*, 381 U.S. at 671 (no recovery permitted for damages resulting from *government's* actions); *Allied Tube*, 486 U.S. at 500 (where "restraint of trade . . . is the result of valid governmental action, *as opposed to private action*," there is immunity) (emphasis added). Having held that plaintiffs' harm

resulted from private action, not government action, the Third Circuit was bound to then apply *Pennington* and *Allied Tube* and hold that the *Noerr-Pennington* doctrine does not apply.

3. The Court Below Has Decided an Important Question of Federal Law That Has Not Been, But Should Be, Definitively Settled by this Court: Whether *Noerr-Pennington* Immunity Should Be Extended To Settlement Agreements With States

The law has long been clear that restraints of trade incorporated into a settlement agreement have no immunity from the Sherman Act. *Broadcast Music, Inc. v. CBS, Inc.*, 441 U.S. 1, 13 (1979) ("*BMI*") (no immunity extends to a consent decree entered into with the Department of Justice nor the acts of private parties contemplated by that decree); *United States v. Singer Mfg. Co.*, 374 U.S. 174 (1963) (settlement agreement that incorporates restraints of trade violate the Sherman Act); *Hartford-Empire Co. v. United States*, 323 U.S. 386, *clarified*, 324 U.S. 570 (1945) (settlement unlawful as part of scheme to monopolize). Two recent decisions by the Circuit Courts of Appeal have also addressed whether the *Noerr-Pennington* doctrine immunizes restraints of trade agreed to in the context of settling litigation. *Primetime 24 Joint Venture v. Nat'l Broadcasting Co., Inc.*, 219 F.3d 92 (2d Cir. 2000) (horizontal agreement cannot be immunized by existence of a common lawsuit); *Andrx Pharm., Inc. v. Biovail Corp.*, 256 F.3d 799 (D.C. Cir. 2001) ("private settlement agreement resolving [ ] patent infringement litigation by substituting a market allocation agreement . . . would not enjoy *Noerr-Pennington* immunity"); *see also In re Cardizem CD Antitrust Litig.*, 105 F. Supp. 2d 618 (E.D. Mich. 2000) (same).

The Opinion does not dispute this general proposition; instead, it sets up a special rule for settlement agreements with states. In doing so, however, the lower court virtually invited review by this Court when it observed that, "[t]he Supreme Court has yet to speak definitively on extending petitioning immunity

to settlement agreements with sovereign states." Pet. App. at 30a. This Court should address this important issue.

In extending the *Noerr-Pennington* doctrine to settlement agreements with sovereign states, the Opinion misapprehended the basic nature of the petitioning process as it pertains to litigation. Adversaries do not petition each other in litigation within the meaning of *Noerr-Pennington*. Rather, they petition the tribunal that they are seeking to resolve their dispute, be it a court, zoning board, taxi commission or other administrative tribunal. In litigating the cases culminating in the MSA, the states and the Majors were not petitioning each other. The states, as adversaries to the Majors, were petitioning the courts to force the Majors to pay them money to reimburse them for healthcare costs, and the Majors, as adversaries to the States, were petitioning those same tribunals for a ruling of no liability. *See Philip Morris v. Blumenthal*, 123 F.3d 103 (2d Cir. 1997).[21]

This Court's ruling in *BMI* rejecting the proposition that a restraint embodied in a consent decree entered into with the Antitrust Division of the Department of Justice entitles the a party to antitrust immunity should be equally applicable to cases where a state or group of states are in litigation. There this Court held:

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21. One observer, critical of the decision below, said:

> The trouble is that 'petitioning' by settling a lawsuit is very different from, say, lobbying one's legislature. Usually, petitioning the government takes place as part of a public debate. Competitors or consumers who might be disadvantaged by what lobbyists are seeking typically have a chance to see what's coming and to voice their objections.
>
> But the tobacco settlement was concocted behind closed doors. Smokers, wholesalers, competitors and others profoundly affected had no opportunity to oppose it. Legislatures and governors had little chance to alter the complex new industry structure the tobacco firms got the attorneys general to approve.

D.J. Tice, "States on Big Tobacco's Side After Smoke Clears," St. Paul Pioneer Press, Aug. 31, 2001.

> Of course, a consent judgment, even one entered at the behest of the Antitrust Division, does not immunize the defendant from liability for actions, including those contemplated by the decree, that violate the rights of nonparties.

BMI, 441 U.S. at 13.

The Opinion sought to distinguish *BMI* by asserting that it did not involve a settlement agreement. Pet. App. at 30a. But a consent decree *is* a settlement agreement. That the settlement becomes embodied in a judicial document and then is so ordered by a judge does not in any way nullify the fact that it is a settlement agreement. Indeed, the MSA envisages that each state will present a consent decree in the form annexed to the MSA as an exhibit. JA 159-60 (MSA § XIII); JA 201-07 (MSA Exh. L). The Opinion also suggests (Pet. App. at 30a-31a) that *BMI* is distinguishable because the issue of *Noerr-Pennington* immunity was not discussed in that case. *Noerr*, however, was decided in 1961, *Pennington* in 1965 and *California Motor Transport Co. v. Trucking Unlimited*, 404 U.S. 508 (1972), in 1972, which removes any doubt that *Noerr-Pennington* covered the conduct of litigation. By 1978, when *BMI* was argued, that doctrine had become well known and firmly embedded in the antitrust law. That the members of this Court as well as the experienced antitrust lawyers in *BMI* recognized the obvious proposition that the Constitutional protection for the petitioning process did not cover deals made between litigants, even when one of the adversaries is a federal government, is no reason for reaching a contrary result when one of the adversaries is a group of states.

Finally, the Opinion's reliance on *Campbell v. Chicago*, 823 F.2d 1182 (7th Cir. 1987) as supporting precedent is misplaced. Pet. App. at 30a-31a. The Seventh Circuit did not "recognize[] the application of *Noerr-Pennington* immunity to settlements between private parties and state government." Pet. App. at 29a-30a. What *Campbell* involved was a suit by a group of taxicab operators as well as their lobbying the City of Chicago

for an ordinance seeking in effect a local monopoly for a group of taxicabs. 823 F.2d at 1183. All the Seventh Circuit held was that the *process* of petitioning the City of Chicago, both by lawsuit and lobbying, was protected activity under *Noerr-Pennington*. *Id.* at 1185-87. When it came to the issue of immunity of the local monopoly resulting from that petitioning, the Seventh Circuit, again quite correctly, held that it was governed by the rules pertaining to the state action doctrine. As the Seventh Circuit stated in *Campbell*:

> It is important to identify the source of the injury to competition. If the injury is caused by persuading the government, then the antitrust laws do not apply to the *squelching* (*Parker v. Brown*) or the *persuasion* (*Noerr-Pennington*).

Id. at 1186. (Emphasis added). The persuasion process in *Campbell*, the petitioning of the courts and lobbying, is *Noerr-Pennington* activity, and the squelching of competition resulting from the local ordinance is classic state action.[22] Thus, *Campbell* does not "resonate[]" with the Opinion's conclusion on *Noerr-Pennington* (Pet. App. at 30a); but conflicts with it.

In summary, the Opinion articulates no defensible rationale for its creation of this new, and, we submit, dangerous expansion of the *Noerr-Pennington* doctrine, which encompass agreements to restrain trade put into settlement agreements made by private firms with states that have sued them.

4. The Court Should Address the Issue of Whether the Supremacy, Commerce and Compact Clauses Preclude *Noerr-Pennington* Immunization of the Interstate Output Cartel

The issues of whether the operation of a cartel controlling the nationwide output of cigarettes constitutes a direct

22. Regulating local cab companies is quintessential local state action activity. *See, e.g., Charley's Taxi Radio Dispatch Corp. v. SIDA of Hawaii*, Inc., 810 F.2d 869 (9th Cir. 1987); *Independent Taxicab Drivers' Employees v. Greater Houston Transp. Co.*, 760 F.2d 607 (5th Cir. 1985).

interference by the collaborating states with interstate commerce and directly conflicts with § 1 of the Sherman Act present two sides of the same coin. The criteria for determining whether a restraint of trade imposed by a state directly interferes with commerce are the same as those used to determine whether it directly conflicts with the Sherman Act. 2 RONALD D. ROTUNDA & NOWAK, *TREATISE ON CONSTITUTIONAL LAW, SUBSTANCE AND PROCEDURE*, § 11.1, at 130-31 (3d ed. 1999). Compare preemption cases such as *Rice v. Norman Williams Co.*, 458 U.S. 654, 659-62 (1982), and *Schwegmann Bros. v. Calvert Distillers Corp.*, *supra*, with *Healy v. Beer Institute, Inc.*, 491 U.S. 324, 332 (1989), holding that a state imposed restraint which "has the 'practical effect' of regulating commerce occurring wholly outside that State's border is invalid under the Commerce Clause."

The direct interference with interstate commerce in violation of the Commerce Clause is at the heart of the issue raised in this case: can the major competitors in an industry collaborate with a group of states to control that nationwide industry by placing restraints in a settlement agreement with those states? The decisional law applying the dormant Commerce Clause indicates that this is impermissible. *See Bacchus Importers, Ltd. v. Dias*, *supra*; *Quill Corp. v. North Dakota*, *supra*; *Brown-Forman Distillers Corp. v. New York State Liquor Auth.*, 476 U.S. 573 (1986).

In addition, the MSA's interference with interstate commerce is exacerbated by its advertising and promotion provisions not only being in direct conflict with the FCLAA, but being an integral discriminatory facet of the implementation of the output cartel. The MSA advertising provisions constitute a sweetheart deal between the Majors and the lawyers for the states by giving the Majors, and no other manufacturers, grandfather rights for brand name sponsorships, giveaways of merchandise and sports promotions. JA 108 (MSA §§ III(c)(2)(ii)); JA 108-09 (MSA § III(c)(3)); JA 110 (MSA § III(f)); JA 111 (MSA § III(i)). No one else gets these deals.

A small manufacturer, however, can only avoid these advertising restrictions in the MSA by becoming an NPM. Thus, a small manufacturer is jammed into a classic Catch-22 quandary. The only way it can avoid the non-deductible penalties imposed on an NPM is to become an SPM. But if it becomes an SPM, it forfeits its First Amendment rights to advertise. Either way the Majors throttle the ability of small companies to compete. This deprivation on an interstate scale of the constitutionally guaranteed advertising advantages and promotional advantages that they would otherwise be legally permitted to enjoy burdens commerce. *See Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511 (1935).

Most importantly, however, the stated objective of the Renegade Clause and the Escrow Statutes of "effectively and fully neutralizing the cost disadvantages" imposed on the Majors directly interferes with interstate commerce. Small manufacturers which are forced to join the MSA as SPM's or to pay penalties imposed by the Escrow Statutes are impermissibly deprived of a substantial cost advantage in interstate commerce. The MSA payments to any given state are determined *solely* by and depend upon an SPM's total sales in interstate commerce, with no relation to the local activity that it conducts in that state. The Escrow Statute penalties paid to any given state reach across state borders to NPM's whose business is confined to another state but whose products are transported and sold in that state by others. The result of penalizing the interstate sales of both SPM's and NPM's to avoid the loss of market share by the Majors that would normally flow from their substantial price increases is the restriction of output on an interstate scale. Such an interstate regulatory scheme is impermissible interference with interstate commerce. *Baldwin*, 294 U.S. at 524 (striking down state law that had the effect of eliminating the competitive advantage enjoyed by Vermont dairy farmers by equalizing the price of milk from all sources, including interstate ones).

The practical effect of the Escrow Statutes, in conjunction with the Renegade Clause "is to create just the kind of competing

and interlocking local economic regulation that the Commerce Clause was meant to preclude." *Healy*, 491 U.S. at 337. The MSA's total regulation of interstate commerce engaged in by *all* makers of U.S. cigarettes clearly violates the Commerce Clause. *See Edgar v. MITE Corp.*, 457 U.S. 624, 642-43 (1982).

This Court should also rule on whether the Compact Clause, U.S. Constitution, Art. I, § 10, cl.3, prohibits the states' mutual surrender of state sovereignty, both to themselves and to the Majors, for the purpose of effectuating this output cartel. In the court below, the Majors argued that the Compact Clause is not violated because it is restricted only to contracts made between the States themselves and not between the States on the one hand and private parties on the other. This Court has never ruled on that issue.

This Court has interpreted the Compact Clause as prohibiting the States from forming, without the consent of Congress, "any combination tending to the increase of political power in the states, which may encroach upon or interfere with the just supremacy of the United States." *United States Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. 452, 468 (1978) (quoting *Virginia v. Tennessee*, 148 U.S. 503, 519 (1893)); *id.* at 471 (same). Under this construction of the Clause, the "relevant inquiry must be one of impact on our federal structure." 434 U.S. at 471. Thus, although a compact clause issue is also akin in large measure to a preemption analysis, it differs in one respect that merits consideration by this Court. Preemption hinges upon a direct conflict between the States and federal law, but a compact made between States without congressional consent is invalid if it "tend[s] to the increase" of state power or if it "may" encroach upon or interfere with federal powers. *Id.* at 493. Consequently, "the pertinent inquiry is one of *potential*, rather than actual, impact on federal supremacy." *Id.* at 472 (emphasis added).

The MSA not only lacks congressional consent but also was made only after Congress rejected the proposed output cartel subsequently embodied in the MSA. Pet. App. at 7a. Thus, in

assessing compliance with the Compact Clause, the question under the test of *United States Steel*, is whether the MSA tends "to the increase of political power in the states, which may encroach upon or interfere with the just supremacy of the United States." 434 U.S. at 468.

Turning to the violation of the Compact Clause, the MSA meets all of the requirements for an unconstitutional interstate compact set forth in *United States Steel Corp.*, 434 U.S. at 473.

1. It interferes with the exercise of powers held by the federal government.
2. It is a surrender of state sovereignty to private parties which are appointed pursuant to the mechanisms set up in the MSA. In the event that a non-severable provision is invalidated, only the Majors, not the states, have the right to terminate the agreement. JA 167-68 (MSA § XVIII(o)).
3. Finally, it allows the states which have joined the agreement to exercise powers that they could not do so in the absence of that agreement. As noted above, both the MSA and the Escrow Statutes explicitly seek to raise revenue on the basis of the interstate business of SPM's and NPM's. That is a power reserved to the federal government.

5. The Court Below Improperly Concluded that The Constitutional Objections To Antitrust Immunity Defenses Were Not Raised in the District Court

The Third Circuit in refusing to rule on these constitutional issues, in effect has given a *sub silentio* blessing to the notion that agreements such as the one presented here do not run afoul of the Commerce, Supremacy or Compact Clauses. The Opinion avoided confronting this unconstitutional encroachment upon the enumerated powers of the present government for two reasons: 1) it ruled that the petitioners had an obligation to raise these objections to the application of *Noerr-Pennington* and state action immunity in their complaint, and 2) that the petitioners did not raise these constitutional issues in the trial

court. Pet. App. at 60a-61a. The first reason is legally untenable and the second factually inaccurate.

With respect to the first reason, the Opinion, in effect, seeks to fashion a new rule of pleading, namely, requiring plaintiffs to raise objections to affirmative defenses in their complaint.[23] The pertinent rule is that allegations in the complaint which seek to avoid or defeat potential affirmative defenses constitute "improper pleading because these allegations are not an integral part of plaintiff's claim." 5 CHARLES ALAN WRIGHT & ARTHUR R. MILLER, *FEDERAL PRACTICE & PROCEDURE*, § 1276 (Civ. 2d 1990).

With respect to the second reason, the Third Circuit is incorrect in asserting that in the trial court the plaintiffs did not argue that the affirmative defenses of antitrust immunity, *i.e.*, both *Noerr-Pennington* and state action immunity were unavailable in light of the invalidity of the MSA under both the Commerce, Compact and Supremacy Clauses. JA 617-21. The Amended Complaint, in fact, challenged the constitutionality of the MSA under both the Commerce Clause and Compact Clause. JA 688 (Am. Cmplt. ¶ 65), JA 698-99 (Am. Cmplt. ¶102). Indeed, the plaintiffs not only raised the unavailability of these affirmative defenses of antitrust immunity in the trial court, but also the Majors' principal argument was that the protection of the right to petition embodied in the *Noerr-Pennington* doctrine overrode any such constitutional infirmities as a direct interference with interstate commerce, a direct conflict with the Sherman Act, or violation of the Compact Clause. JA 624-627. Although the Third Circuit did not discuss the issue of preemption under the Supremacy Clause, *i.e.*, a direct conflict with § 1 of the Sherman Act, that issue was also raised by petitioners as a reason for rejecting the applicability of *Noerr-Pennington* doctrine in both the Third Circuit and the trial

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23. The *Noerr-Pennington* immunity claim is, of course, an affirmative defense. *Bayou Fleet, Inc. v. Alexander*, 234 F.3d 852, 860 (5th Cir. 2000), *cert. denied*, 121 S. Ct. 1228 (2001); *North Carolina Elec. Membership Corp. v. Carolina Power & Light Co.*, 666 F.2d 50, 52 (4th Cir. 1981).

court.[24] Moreover, both petitioners' main brief in the Third Circuit (at 30), as well as their reply brief (at 14 at n.10) pointed out these issues of unconstitutionality had been raised in the court below as reasons for the unavailability of the *Noerr-Pennington* doctrine.

Petitioners submit as to whether the MSA violates these constitutional protections against interference by the States with the national economy is a matter of national significance which the Court should decide.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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24. With respect to the trial court proceedings, the violations of the Constitution were pleaded in the Amended Complaint at paragraphs 65 and 102 (JA 688, 698), and Plaintiffs' Brief in Opposition to Motion to Dismiss, Docket No. 27, citing and relying on the seminal case on Sherman Act preemption, *Northern Securities Co. v. United States*, 193 U.S. 197, 345 (1904) at 4 and 18 at n. 21 (JA 620), as well as *Schwegmann Bros. v. Calvert Distillers Corp.*, *supra*, at 7. With respect to the proceedings in the Third Circuit, *see* Plaintiffs' Opening Brief at 52-53, citing and discussing *Northern Securities* and *Rice v. Norman Williams*, 458 U.S. 654 (1982); Reply Brief at 2, 4 and 15, also citing and discussing *Northern Securities* and *Rice*.

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APPENDIX A — OPINION AND JUDGMENT OF THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT DATED AND FILED JUNE 19, 2001

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 00-3410

A.D. BEDELL WHOLESALE COMPANY, INC.;
TRIANGLE CANDY & TOBACCO CO., on behalf of themselves and all others similarly situated,

Appellants

v.

PHILIP MORRIS INCORPORATED;
R.J. REYNOLDS TOBACCO COMPANY, INC.;
BROWN AND WILLIAMSON TOBACCO CORP.

On Appeal from the United States District Court
for the Western District of Pennsylvania
D.C. Civil Action No. 99-cv-00558
(Honorable Donetta W. Ambrose)

Argued December 14, 2000

Before: SCIRICA, FUENTES and GARTH,
Circuit Judges

(Filed JUN 19 2001)

* * *

Appendix A

OPINION OF THE COURT

SCIRICA, *Circuit Judge.*

This is an appeal from the dismissal under Fed. R. Civ. P. 12(b)(6) of claims brought under the Sherman Antitrust Act attacking the multi-billion dollar national tobacco settlement. Endeavoring to recoup billions of dollars in public health care costs and to reduce cigarette smoking, several states brought suit against the leading United States tobacco manufacturers. In view of the magnitude of potential liability and the prospect of multiple actions, the parties asked Congress to resolve the suits through a national legislative remedy. After congressional efforts stalled, forty-six states[1] forged a settlement with the tobacco manufacturers known as the Multistate Settlement Agreement. Plaintiffs, who are cigarette wholesalers, challenge the Multistate Settlement Agreement as a violation of § 1 and § 2 of the Sherman Antitrust Act.[2]

The District Court held that plaintiffs failed to state a claim under the Sherman Act because the tobacco companies

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1. Forty-six states and six other U.S. jurisdictions (District of Columbia, Puerto Rico, Virgin Islands, American Samoa, Guam and the Northern Mariana Islands) signed the agreement. Four states (Florida, Minnesota, Mississippi, and Texas) entered into prior separate settlements with the tobacco companies and are thus not signatories to the Multistate Settlement Agreement. *PTI, Inc. v. Philip Morris, Inc.*, 100 F.Supp.2d 1179, 1185 n.2 (C.D. Cal. 2000).

2. These portions of the Sherman Act are codified at 15 U.S.C. §§ 1, 2. A claim under § 7 of the Clayton Act, 15 U.S.C. § 18, was voluntarily dismissed without prejudice.

were immune from antitrust liability under both the *Noerr-Pennington*[3] and *Parker*[4] immunity doctrines.[5] We agree they are immune under the *Noerr-Pennington* doctrine but not under the *Parker* doctrine. We will affirm.[6]

I.

Facts and Procedural History

A.D. Bedell, a cigarette wholesaler, brought this class action on behalf of itself and 900 similarly situated wholesalers seeking damages and a permanent injunction of the Multistate Settlement Agreement. Defendants, Philip Morris, Inc., R.J. Reynolds Tobacco Co., Inc., and Brown & Williamson Tobacco Corp., are cigarette manufacturers who were original signatories to the Multistate Settlement Agreement.[7]

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3. *E. R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127 (1961); *United Mine Workers v. Pennington*, 381 U.S. 657 (1965).

4. *Parker v. Brown*, 317 U.S. 341, 352 (1943).

5. *A.D. Bedell Wholesale Co., Inc. v. Philip Morris, Inc.*, 104 F.Supp.2d 501 (W.D. Pa. 2000).

6. The District Court had subject matter over these federal claims under 15 U.S.C. §§ 15, 26 as well as under 28 U.S.C. § 1331. We have jurisdiction over this appeal of dismissal under Fed. R. Civ. P. 12(b)(6) pursuant to 28 U.S.C. § 1291.

7. Amicus Briefs were filed by Attorneys General from signatory states supporting the tobacco companies and from the Cato Institute supporting plaintiffs.

Appendix A

Along with Lorillard Tobacco Co.,[8] the fourth largest cigarette producer, they are collectively known as the major tobacco companies or the Majors. The Majors are responsible for 98% of cigarette sales in the United States. Bedell, as a wholesaler, bought directly from the Majors.

In the mid 1990's, individual states commenced bringing law suits against the Majors to recoup healthcare costs and reduce smoking by minors.[9] As one state Attorney General declared, " '[The] lawsuit is premised on a simple notion: you caused the health crisis; you pay for it.' " Janofsky, *Mississippi Seeks Damages from Tobacco Companies*, N.Y. Times, May 24, 1994, at A12 (quoting Mississippi Attorney General Mike Moore). The States alleged a wide range of deceptive and fraudulent practices by the tobacco companies over decades of sales.[10] Faced with the prospect of defending

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8. Lorillard is not named as a defendant, but is an original participating manufacturer.

9. *See* Michael Janofsky, *Mississippi Seeks Damages From Tobacco Companies*, N.Y. Times, May 24, 1994, at A12 ("Mississippi today became the first state to demand that cigarette makers bear the health care costs of smoking."); Gordon Slovut, *State, Blue Cross Sue Tobacco Industry*, Star Tribune, August 18, 1994, at A1 (stating Minnesota filed suit against the tobacco industry); Andrew Wolfson, *West Virginia Takes on Tobacco Over Health Costs*, The Courier-Journal, Sept. 22, 1994, at A1; Amy Goldstein, *Maryland to Sue Makers of Cigarettes: Effect of Smoking on Medicaid at Issue*, Washington Post, Nov. 17, 1995, at B1 (reporting Maryland Governor Parris Glendening's announcement of decision to sue tobacco companies).

10. For example, Pennsylvania brought suit alleging a "conspiracy in concealing and misrepresenting the addictive and

(Cont'd)

multiple actions nationwide, the Majors sought a congressional remedy, primarily in the form of a national legislative settlement.[11] In June 1997, the National Association of Attorneys General and the Majors jointly petitioned Congress for a global resolution.

The proposed congressional remedy (1997 National Settlement Proposal) for the cigarette tobacco problem resembled the eventual Multistate Settlement Agreement, but with important differences. For example, although the congressional proposal would have earmarked 1/3 of all funds to combat teenage smoking, no such restrictions appear in the Multistate Settlement Agreement. 1997 National Settlement Proposal, Title VII, *available at* http://www.cnn.com/us/9705/tobacco/docs/proposal.html (last visited June 18, 2001). In addition, the congressional proposal would have mandated Food & Drug Administration

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harmful nature of tobacco/nicotine[,] . . . industry control and manipulation of nicotine to foster addiction and thus profits[,] . . . intentionally attracting and addicting children to tobacco products," and "targeting African Americans." (complaint in *Commonwealth of Pennsylvania v. Philip Morris, Inc.*). These claims encompass civil conspiracy, willful and negligent breach of a special duty, fraudulent misrepresentation, fraudulent concealment, negligent design, strict liability, unfair trade practices, public nuisance, and negligent and intentional entrustment.

11. As of October 1996, sixteen states had brought suit. *See Utah Sues Tobacco Companies*, The Washington Post, Oct. 1, 1996, at A9 (reporting Utah joined fifteen other states, along with many counties and cities, in filing lawsuits against major tobacco companies).

oversight and imposed federal advertising restrictions. It also would have granted immunity from state prosecutions; eliminated punitive damages in individual tort suits; and prohibited the use of class actions, or other joinder or aggregation devices without the defendant's consent, assuring that only individual actions could be brought. *See id.* at Title V(A), VIII(A), VIII(B). The congressional proposal called for payments to the States of $368.5 billion over twenty-five years. 1997 National Settlement Proposal, Title VI.[12] By contrast, assuming that the Majors would maintain their market share, the Multistate Settlement Agreement provides baseline payments of about $200 billion over twenty-five years.[13] *See* Multistate Settlement Agreement, §§ IX(a), (b), (c).

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12. Because the congressional proposal also would have involved much higher payments by the Majors (by up to $170 billion), it was expected that cigarette prices would increase $.60/pack. *See* FTC Report on Competition and the Financial Impact of the Proposed National Tobacco Settlement 34 (September 1997).

13. This baseline payment is subject to

> the Inflation Adjustment, the Volume Adjustment, the Previously Settled States Reduction, the Non-Settling States Reduction, the NPM Adjustment, the offset for miscalculated or disputed payments described in subsection XI(i), the Federal Tobacco Legislation Offset, the Litigating Releasing Parties Offset, and the offsets for claims over described in subsections XII(a)(4)(B) and XII(a)(8).

MSA § IX(c).

Appendix A

Significantly for our purposes, the congressional proposal included an explicit exemption from the federal antitrust laws. *See* 1997 National Settlement Proposal, App. IV(C)(2) (stating cigarette manufacturers would have been permitted to "jointly confer, coordinate or act in concert, for this limited purpose [of achieving the goals of the settlement]"). The Multistate Settlement Agreement contains no corresponding exemption from the federal antitrust laws.

Congress rejected the proposed settlement in the spring of 1998.[14] Undeterred, the State Attorneys General and the Majors continued to negotiate and on November 23, 1998, they executed the Multistate Settlement Agreement. Afterwards, twenty other tobacco manufacturers, representing 2% of the market, joined the settlement as Subsequent Participating Manufacturers (SPMs). The addition of the Subsequent Participating Manufacturers meant that nearly all of the cigarette producers in the domestic market had signed the Multistate Settlement Agreement. Their addition was significant. The Majors allegedly feared that any cigarette manufacturer left out of a settlement (Non-Participating Manufacturers or NPMs) would be free to expand market share or could enter the market with lower prices, drastically altering the Majors' future profits and their ability to increase prices to pay for the settlement.

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14. An alternative settlement, proposed by Senator John McCain of Arizona, which included even higher payments from the industry ($500 billion) and would not have provided antitrust exemptions was also defeated, and along with it the prospects of a federal solution.

Appendix A

Plaintiffs brought suit challenging sections of the Multistate Settlement Agreement allegedly designed to maintain market share and restrict entry. The challenged sections of the Multistate Settlement Agreement are the so-called "Renegade Clause,"[15] the settlement's primary mechanism for allocating payment responsibilities based on production levels, and the provision calling for "Qualifying Statutes," which are state laws passed as a result of commitments made in the Multistate Settlement Agreement that require Non-Participating Manufacturers to pay into state escrow accounts for each sale made. Plaintiffs claim the Multistate Settlement Agreement and resulting state implementing statutes create an output cartel that imposes draconian monetary penalties for increasing cigarette production beyond 1998 levels and effectively bars new entry into the cigarette market.

The Renegade Clause allegedly was designed to prevent current cigarette manufacturers from decreasing prices to increase market share and to bar new entrants from the market.[16]

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15. Small cigarette producers (who generally sell at a discount) are referred to as "Renegades." The "Renegade Clause" incorporates two distinct sections of the Multistate Settlement Agreement, one part deals with Non-Participating Manufacturers or NPMs, the other with Subsequent Participating Manufacturers or SPMs. *See* MSA §§ IX(i) (SPMs), (d) (NPMs). The Attorneys General object to the appellation "Renegade" claiming that only voluntary signatories are affected by its provisions. But there are penalties imposed on non-signatories under the Qualifying Statutes which each State must try to implement in accordance with the Multistate Settlement Agreement.

16. There were similar provisions in the congressional proposal designed to restrict Non-Participating Manufacturers (NPMs). (Cont'd)

Appendix A

One part of the Renegade Clause affects tobacco companies (SPMs) that later join the Multistate Settlement Agreement. This section creates strong disincentives for Subsequent Participating Manufacturers to increase their production and market share. If a Subsequent Participating Manufacturer exceeds its 1998 market share (or exceeds 125% of 1997 market share if that is greater), then it must pay into the settlement fund.[17] By maintaining historic market share, it would owe nothing to the settlement fund. For every carton of cigarettes sold in 1999 over its 1998 level, a SPM would have to pay $.19/pack into the settlement fund. Plaintiffs contend this equaled 75% of the wholesale price, which defendants do not contest. *See* Br. of Appellants at 14 (applying MSA § IX(C)); MSA Ex. E. This mechanism allegedly discourages Subsequent Participating Manufacturers from underpricing the Majors to increase market share, even if they could efficiently do so.

Another part of the Renegade Clause affects Non-Participating Manufacturers (NPMs), cigarette companies

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These provisions provided for escrow payments and also subjected them to the broad regulatory authority that would have been created under the proposal. *See* 1997 National Settlement Proposal, Title II, Part C.

17. The Multistate Settlement Agreement provides, "A Subsequent Participating Manufacturer shall have payment obligations under this Agreement only in the event that its Market Share in any calendar year exceeds the greater of (1) its 1998 Market Share or (2) 125 percent of its 1997 Market Share." MSA § IX(i)(1). These payments "are in addition to the corresponding payments that are due from the Original Participating Manufacturers." MSA § IX(i)(1).

that never sign the Multistate Settlement Agreement. Non-Participating Manufacturers include potential new entrants into the tobacco market. *See* MSA § IX(d). But as noted, between the SPMs and the Majors, about 99% of the current cigarette producers signed the Multistate Settlement Agreement. The strictures of the Multistate Settlement Agreement affecting NPMs were largely responsible for such participation. Potential new entrants into the cigarette market would bear the burden of the Renegade Clause's future effects.

Under the Renegade Clause, if Non-Participating Manufacturers gain market share (thereby reducing the Majors' market share) the Majors may decrease their principal payments to the settlement fund. If the Majors lose market share to NPMs, the payments to the settlement fund are not merely reduced proportionately. *See* MSA § IX(d)(1)(A) & (B). For example, if a participating tobacco company lost 10% of its market share to a new entrant or other company that did not sign the Multistate Settlement Agreement, it may be able to reduce its payments by as much as 24%. *See* Hanoch Dagan & James J. White, *Governments, Citizens, and Injurious Industries*, 75 N.Y.U. L. Rev. 354, 381 (2000) (making hypothetical calculations based on the formulas in MSA § IX(d)).[18]

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18. Section IX(d) of the Multistate Settlement Agreement describes the calculation of the NPM adjustment as follows:

(d) *Non-Participating Manufacturer Adjustment*

(1) *Calculation of NPM Adjustment for Original Participating Participant*

(Cont'd)

Appendix A

(Cont'd)

Manufacturers. To protect the public health gains achieved by this Agreement, certain payments made pursuant to this Agreement shall be subject to an NPM Adjustment. Payments by the Original Participating Manufacturers to which the NPM Adjustment applies shall be adjusted as provided below:

(A) Subject to the provisions of subsections (d)(1)(C), (d)(1)(D) and (d)(2) below, each Allocated Payment shall be adjusted by subtracting from such Allocated Payment the product of such Allocated Payment amount multiplied by the NPM Adjustment Percentage. The "NPM Adjustment Percentage" shall be calculated as follows;

(i) If the Market Share Loss for the year immediately preceding the year in which the payment in question is due is less than or equal to 0 (zero), then the NPM Adjustment Percentage shall equal zero.

(ii) If the Market Share Loss for the year immediately preceding the year in which the payment In question is due is greater than 0 (zero) and less than or equal to 16 2/3 percentage points, then

(Cont'd)

Appendix A

By enacting the Qualifying Statute set forth in the Multistate Settlement Agreement, *see* MSA Ex. T, a state can preclude reduced payments.[19] The model statute provides,

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> the NPM Adjustment Percentage shall be equal to the product of (x) such Market Share Loss and (y) 3 (three).
>
> (iii) If the Market Share Loss for the year immediately preceding the year in which the payment in question is due is greater than 16 2/3 percentage points, then the NPM Adjustment Percentage shall be equal to the sum of (x) 50 percentage points and (y) the product of (1) the Variable Multiplier and (2) the result of such Market Share Loss minus 16 2/3 percentage points.

The remainder of § IX(d) gives definitions for some of the terms and describes who will make this calculation and when it will be made each year, as well as how the adjusted payments will be allocated among the States and the signatories. *See* MSA § IX(d).

19. The Multistate Settlement Agreement provides:

> (B) A Settling State's Allocated Payment shall not be subject to an NPM Adjustment: (i) if such Settling State continuously had a Qualifying Statute (as defined in subsection (2)(E) below) in full force and effect during

(Cont'd)

Appendix A

> Any tobacco product manufacturer selling cigarettes to consumers within the State . . . after the date of enactment of this Act shall do one of following:
>
> (a) become a participating manufacturer (as that term is defined in section II(jj) of the Master Settlement Agreement) and generally perform its financial obligations under the Master Settlement Agreement; or
>
> (b)(1) place into a qualified escrow fund . . . the following amounts . . . .

Id. The model Qualifying Statute would impose a tax on new tobacco entrants of approximately $.27/pack in the year 2001,

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> the entire calendar year preceding the year in which the payment in question is due and diligently enforced the provisions of such statute during such entire calendar year; or (ii) such Settling State enacted the Model Statute (as defined in subsection (2)(E) below) for the first time during the calendar year immediately preceding the year in which the payment in question is due, continuously had the Model Statute in full force and effect during the last six months of such calendar year, and diligently enforced the provisions of such statute during the period in which it was in full force and effect.

MSA § IX(d)(2)(B). Aside from the financial incentive, the Multistate Settlement Agreement also encourages the States to enact the Qualifying Statutes. *See* MSA § IX(d)(2)(E).

rising to $.36/pack by the year 2007. *See* MSA Ex. T. A Non-Participating Manufacturer only can recover its deposited funds: (1) if it is forced to pay a judgment or settlement in connection with a claim brought by the state, or (2) after the passage of twenty years free from any such judgments. *See id.* Because the Non-Participating Manufacturers are not part of the settlement, they have no immunity and would be subject to similar suits brought by the State Attorneys General against the Majors (for fraudulent concealment, misrepresentation, conspiracy, etc.). To encourage and assist the States in bringing these suits, the Multistate Settlement Agreement created a $50 million Enforcement Fund (paid for by the Majors) to investigate and sue NPMs to enforce the settlement. *See* MSA § VIII(c). Because of the Qualifying Statutes, a Non-Participating Manufacturer must decide either to join the Multistate Settlement Agreement and abide by the same restrictions on market share facing a SPM (which for new manufacturers would be costly because they would have a baseline production level of zero), or face litigation and pay a tax into a state-established escrow account for any potential adverse judgments.

Together, the Renegade Clause, the Qualifying Statutes and the Enforcement Fund allegedly create severe obstacles to market entry, or to increasing production and market share.[20] This is not accidental. The Multistate Settlement

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20. Because this is an appeal from a dismissal under Fed. R. Civ. P. 12(b)(6). we address only the complaint's allegations. But we note that news reports have stated that although the Multistate Settlement Agreement was designed to frustrate new cigarette market

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Agreement explicitly proclaims its purpose to reduce the ability of non-signatory cigarette manufacturers to seize market share because of the competitive advantage accruing from not contributing to the settlement. It declares that the agreement "effectively and fully neutralizes the cost disadvantages that the Participating Manufacturers experience vis-à-vis Non-Participating Manufacturers with such Settling States as a result of the provisions of this Agreement." MSA § IX(d)(2)(E).

It is these barriers to entry and increased production that plaintiffs claim form an output cartel that violates the antitrust laws. Because output is restricted and because of the inelastic demand for cigarettes,[21] in part due to their addictive nature, the Multistate Settlement Agreement allegedly permitted the Majors to raise their prices to near monopoly levels — levels allegedly above those necessary to fund the settlement payments. For example, assert plaintiffs, the settlement could have been funded by only a $.19/pack increase in price, but the Majors immediately raised prices by $.45/pack, and subsequently by another

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entrants, it appears that some new discount cigarette manufacturers have been able to enter the market. Gordon Fairclough, *Tobacco Deal Has Unintended Effect: New Discount Smokes*, Wall St. J., May 1, 2001, at A1. Some new entrants apparently have failed to make required payments into escrow accounts as required by the state enacted Qualifying Statutes. Others apparently have accepted significantly lower profit margins. *See id.*

21. Demand for a product is inelastic if the price can rise without a corresponding drop in demand.

$.31/pack.[22] When this lawsuit was filed, the Majors had already raised the wholesale price of cigarettes $.76/pack since the adoption of the Multistate Settlement Agreement. Rapid price increases of this magnitude would ordinarily permit competitors to maintain or reduce prices or prompt new competitors to enter the market. But neither occurred, assert plaintiffs, because the barriers erected by the Multistate Settlement Agreement effectively barred entry and discouraged tobacco companies from maintaining a lower price because of the penalties for increased production.

Defendants contend the Multistate Settlement Agreement did not violate the antitrust laws, but even if so, they are immune under both the *Noerr-Pennington* doctrine, which protects petitioning activity, and the *Parker* doctrine, which protects sovereign acts of states from antitrust liability. We turn first to the antitrust issues.

II.

Antitrust Injury

The defendants argue the express terms of the Multistate Settlement Agreement do not constitute an agreement to limit output in violation of the antitrust laws. Plaintiffs counter that the Multistate Settlement Agreement's Renegade Clause,

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22. *See* Vanessa O'Connell, *Philip Morris, RJR Lift Wholesale Price For Cigarettes 45 Cents a Pack Today*, Wall St. J., November 24, 1998, at A1; Gordon Fairclough, *Major Makers of Cigarettes Raise Prices*, Wall St. J., August 31, 1999, at A3 ($.18/pack increase); Gordon Fairclough, *Philip Morris Boosts Prices of Cigarettes*, Wall St. J., January 17, 2000, at B12 ($.13/pack increase).

Qualifying Statutes, and Enforcement Fund, have the "unequivocal purpose and effect" to "effectuate a cartel limiting the output of cigarettes, thereby allowing the Majors to maintain supracompetitive prices," which is a per se violation of the antitrust laws. Br. of Appellants at 29.

To maintain a cause of action under the Sherman Act, "[p]laintiffs must prove *antitrust* injury, which is to say (1) injury of the type the antitrustlaws were intended to prevent and (2) that flows from that which makes defendants' acts unlawful." *Brunswick Corp. v. Pueblo Bowl-O-Mat*, 429 U.S. 477, 489 (1997) (emphasis in original). The antitrust injury requirement "ensures that the harm claimed by the plaintiff corresponds to the rationale for finding a violation of the antitrust laws in the first place, and it prevents losses that stem from competition from supporting suits by private plaintiffs." 2 Philip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 362 (Rev. ed. 1997).

Here, the losses plaintiffs allege resulted from explicit provisions of the Multistate Settlement Agreement, not from competition. Plaintiffs allege the major tobacco companies formed and enforced a cartel to restrict output through the Multistate Settlement Agreement. As a result, plaintiffs claim the Majors "imposed artificially high prices on direct purchasers," without fear of competition. *See* Complaint ¶ 2. Although this result would affect cigarette prices for retailers and consumers, as well as for wholesalers like plaintiffs, the Supreme Court has determined that direct buyers are the only parties with standing to assert damage claims under the antitrust laws for overcharges based on an output cartel. *Ill. Brick Co. v. Illinois*, 431 U.S. 720, 734

(1977) ("[T]he antitrust laws will be more effectively enforced by concentrating the full recovery for the overcharge in the direct purchasers rather than by allowing every plaintiff potentially affected by the overcharge to sue only for the amount it could show was absorbed by it."). Although plaintiffs, as wholesalers, have alleged an injury, they must also demonstrate that the conduct which caused the injuries violated the antitrust laws.

An agreement which has the purpose and effect of reducing output is illegal under § 1 of the Sherman Act. *Cal. Dental Ass'n v. FTC*, 526 U.S. 756, 777 (1999) (output restrictions are anticompetitive); *Nat'l Collegiate Athletic Ass'n v. Bd. of Regents of Univ. of Okla.*, 468 U.S. 85, 99 (1984) (where "the challenged practices create a limitation on output; our cases have held that such limitations are unreasonable restraints of trade") (citing *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 608-09 (1972)); *United States v. Sacony-Vacuum Oil Co.*, 310 U.S. 150, 223 (1940). In *California Dental*, the Court restated that output restrictions are anticompetitive. At the same time, it refused to apply a "quick look analysis" where a local professional association had restricted certain types of advertising, but it was not obvious that the restrictions would be anticompetitive.[23] Remanding for further analysis, the Court

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23. A "quick-look" analysis under the rule of reason, may be used when "an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers and markets," yet the violation is also not one considered illegal per se. *Cal. Dental Ass'n*, 526 U.S. at 770. We need not address whether the output cartel

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acknowledged that a reduction in output was an antitrust violation. *Cal. Dental Ass'n*, 526 U.S. at 777, 781. The Court cited with approval a case from the Court of Appeals of the Seventh Circuit which held that if " 'firms restrict output directly, price will rise in order to limit demand to the reduced supply. Thus, with exceptions not relevant here, raising price, reducing output, and dividing markets have the same anticompetitive effects.' " *Id.* at 777 (quoting *General Leaseways, Inc. v. Nat'l Truck Leasing Ass'n*, 744 F.2d 588, 594-95 (7th Cir. 1984)). The Court has made clear that a pure restriction on output is anticompetitive and in the absence of special circumstances,[24] would violate the antitrust

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alleged here would be illegal per se or would be illegal under a "rule of reason" analysis. As the Supreme Court has held:

> The truth is that our categories of analysis of anticompetitive effect are less fixed than terms like 'per se,' 'quick look,' and 'rule of reason' tend to make them appear. We have recognized, for example, that 'there is often no bright line separating per se from rule of reason analysts,' since 'considerable inquiry into market conditions' may be required before the application of any so-called 'per se' condemnation is justified.

Id. at 779 (quoting *NCAA*, 468 U.S. at 104 n.26). " '[W]hether the ultimate finding is the product of a presumption or actual market analysis, the essential inquiry remains the same — whether or not the challenged restraint enhances competition.' " *Id.* at 779-80 (quoting *NCAA*, 468 U.S. at 104).

24. *See, e.g.*, *NCAA*, 468 U.S. at 85 (holding where there is an intrinsic need for output restrictions to ensure a market for the product at all, the restriction may not violate the antitrust laws).

laws. *NCAA*, 468 U.S. at 85 (recognizing that output restrictions may be permissible if required in order to market the product at all). By limiting production, the cartel is able to raise prices above competitive levels.

Federal Trade Commission/Department of Justice Guidelines also recognize that agreements to reduce output violate the antitrust laws. *See* FTC/DOJ Guidelines — Antitrust Guidelines for Collaborations Among Competitors, § 3.2, *reprinted in* 4 Trade Reg. Rep. (CCH) ¶ 20 (2000) (citing *Broadcast Music Inc. v. Columbia Broad. Sys.*, 441 U.S. 1, 19-20 (1979)). These regulations define output agreements as "hard core cartel agreements" and violators are prosecuted criminally without regard to "claimed business purposes, anticompetitive harms, procompetitive benefits, or overall competitive effects." *Id.*

Plaintiffs allege the agreement between the States and the Majors purposefully creates powerful disincentives to increase cigarette production. Although the Multistate Settlement Agreement contains no explicit agreement to raise prices or restrict market share, any signatory who increases production beyond historic levels automatically will increase its proportionate share of payments to the Multistate Settlement Agreement. Normally, a company which lowers prices would be expected to increase market share. But the penalty of higher settlement payments for increased market share would discourage reducing prices here. For this reason, signatories have an incentive to raise prices to match increases by competitors. It appears this incentive structure has proven true. The Majors' prices increased dramatically and simultaneously after signing the Multistate Settlement

Agreement. As noted, this included a $.45/pack increase just days after the settlement was announced, an $.18/pack increase less than a year later, and a $.13/pack increase in January of 2000. The initial $.45 increase alone was more than double what some analysts considered necessary to fund the settlement's first two annual payments. *See* Stuart Taylor Jr., *All for Tobacco and Tobacco for All*, 23 Legal Times 40, Oct. 9, 2000.

Defendants contend an antitrust analysis is unnecessary if we find either *Noerr-Pennington* or *Parker* immunity applies. But plaintiffs argue that immunity cannot attach to per se antitrust violations. We disagree. Recently we recognized immunity attached even where the plaintiff alleged a boycott regarded as illegal per se. *Armstrong Surgical Ctr. Inc. v. Armstrong County Mem'l Hosp.*, 185 F.3d 154, 157-58 (3d Cir. 1999) (applying *Parker* and *Noerr-Pennington* immunity where complaint alleged a threat of a boycott which would have constituted an antitrust violation in the absence of immunity), *cert. denied*, 530 U.S. 1261 (2000). Similarly, in *Pennington*, the alleged conduct granted immunity would have been a per se violation of the antitrust laws. *United Mine Workers v. Pennington*, 381 U.S. 657, 660-61 (1965).

Our review at this stage is limited to the allegations in plaintiffs' complaint. On a motion to dismiss under Fed. R. Civ. P. 12(b)(6), the issue is whether plaintiffs have properly pleaded an antitrust violation.[25] Plaintiffs allege that

25. We exercise de novo review over dismissal of claims under Fed. R. Civ. P. 12(b)(6). *Wilson v. Quadramed Corp.*, 225 F.3d

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defendants formed an output cartel through the Multistate Settlement Agreement that restricts production and effectively bars entry to the cigarette tobacco market. Plaintiffs also allege the cartel injured the tobacco wholesalers by charging artificially high prices.[26]

We hold that plaintiffs have properly pleaded an antitrust violation by alleging defendants agreed to form an output cartel through the Multistate Settlement Agreement that violates § 1 and § 2[27] of the Sherman Antitrust Act. But we

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350, 353 (3d Cir. 2000). In evaluating the propriety of the dismissal, we examine all factual allegations and all reasonable inferences as true and view them in the light most favorable to the plaintiff. *Colburn v. Upper Darby Tp.*, 838 F.2d 663, 666 (3d Cir. 1988). A court may dismiss a plaintiff's complaint only if the plaintiff can prove no set of facts which would entitle him to relief. *Conley v. Gibson*, 355 U.S. 41, 45 (1957).

26. Defendants do not dedicate much of their argument to contesting the antitrust injury, perhaps because the District Court did not address it. The District Court found it unnecessary to decide whether plaintiffs properly pleaded an antitrust violation if it held defendants immune. *A.D. Bedell Wholesale Co., Inc. v. Philip Morris, Inc.*, 104 F.Supp.2d 501, 503 (W.D. Pa. 2000).

27. Section 2 of the Sherman Act applies to, "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations . . . ." 15 U.S.C. § 2. Parties violate § 2 if they are involved in "(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as
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will affirm if the parties to the Multistate Settlement Agreement are immune under the *Noerr-Pennington* or the *Parker* doctrines. We turn now to that question.

III.

Antitrust Immunity

Defendants contend they are immune from antitrust liability under both the *Noerr-Pennington* doctrine, which immunizes parties involved in petitioning the government, and under the *Parker* doctrine, which immunizes sovereign state action. Although distinct doctrines, there is substantial overlap as both "work at the intersection of antitrust and governance."[28] The two doctrines share a fundamental similarity. The Supreme Court has stated they are "complementary expressions of the principle that the antitrust

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distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident." *United States v. Grinnell Corp.*, 384 U.S. 563, 570-71 (1966); *see also Weiss v. York Hosp.*, 745 F.2d 786, 825 (3d Cir. 1984). Here, plaintiffs properly pleaded such a violation. Plaintiffs allege that the Multistate Settlement Agreement creates a cartel controlling 99.9% of the market, giving Philip Morris "the greatest market or monopoly power — i.e. the power to raise prices or decrease output." Complaint at ¶ 98. Plaintiffs also allege Philip Morris had the specific intent to monopolize the cigarette market and has done so. Complaint at ¶ 99. Immunity, if found, will apply to violations of both § 1 and § 2.

28. David McGowan & Mark A. Lemley, *Antitrust Immunity: State Action and Federalism, Petitioning and the First Amendment*, 17 Harv. J.L. & Pub. Pol'y 293, 300 (1994).

laws regulate business, not politics; *Parker* protects the States' acts of governing, and *Noerr* the citizens' participation in government." *City of Columbia v. Omni Outdoor Adver. Inc.*, 499 U.S. 365, 383 (1991). The District Court found defendants immune under both. We must affirm if defendants are immune under either doctrine.

A. *Noerr-Pennington* Immunity

Under the *Noerr-Pennington* doctrine, "[a] party who petitions the government for redress generally is immune from antitrust liability." *Cheminor Drugs, Ltd. v. Ethyl Corp.*, 168 F.3d 119, 122 (3d Cir.), *cert. denied*, 528 U.S. 871 (1999). Petitioning is immune from liability even if there is an improper purpose or motive.[29] *See E. R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 138 (1961) (holding that even if the petitioner's sole purpose was to destroy its competition through passage of legislation, petitioner would be immune); *Prof'l Real Estate Investors, Inc. v. Columbia Pictures Indus., Inc.*, 508 U.S. 49, 56 (1993) (same). Rooted in the First Amendment and fears about the threat of liability chilling political speech, the doctrine was first recognized in two Supreme Court cases holding federal antitrust laws inapplicable to private parties who attempted to influence government action — even where the petitioning had anticompetitive effects. *See Noerr*, 365 U.S. 127 ; *United Mine Workers v. Pennington*, 381 U.S. 657 (1965). Under

29. There is a "sham" exception to the *Noerr-Pennington* doctrine which holds that using the petitioning process simply as an anticompetitive tool without legitimately seeking a positive outcome to the petitioning destroys immunity. *See Omni*, 499 U.S. 365. There is no suggestion that the sham exception applies here.

the *Noerr-Pennington* doctrine, "mere attempts to influence the Legislative Branch for the passage of laws or the Executive Branch for their enforcement" are given immunity from the Sherman Act and other antitrust laws. *Cal. Motor Transp. Co. v. Trucking Unlimited*, 404 U.S. 508, 510 (1972). The immunity reaches not only to petitioning the legislative and executive branches of government, but "the right to petition extends to all departments of the Government," including the judiciary. *Id.*

Noerr-Pennington immunity applies to actions which might otherwise violate the Sherman Act because "[t]he federal antitrust laws do not regulate the conduct of private individuals in seeking anticompetitive action from the government." *Omni*, 499 U.S. at 379-80. The antitrust laws are designed for the business world and "are not at all appropriate for application in the political arena." *Noerr*, 365 U.S. at 141. This was evident in *Noerr*, where defendant railroads campaigned for legislation intended to ruin the trucking industry. Even though defendants employed deceptive and unethical means, the Supreme Court held that they were still immune. This is because the Sherman Act is designed to control "business activity" and not "political activity." *Id.* at 129. With this underpinning, the Court stated, "[Because] [t]he right of petition is one of the freedoms protected by the Bill of Rights, . . . we cannot, of course, lightly impute to Congress an intent to invade these freedoms." *Noerr*, 365 U.S. at 136. The antitrust laws were enacted to regulate private business and do not abrogate the right to petition.

The scope of *Noerr-Pennington* immunity, however, depends on the "source, context, and nature of the

competitive restraint at issue." *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 499 (1988). If the restraint directly results from private action there is no immunity. *See id.* at 500 (where the "restraint upon trade or monopolization is the result of valid governmental action, as opposed to private action," there is immunity). Passive government approval is insufficient. Private parties cannot immunize an anticompetitive agreement merely by subsequently requesting legislative approval.

Under the *Noerr-Pennington* doctrine, private parties may be immunized against liability stemming from antitrust injuries flowing from valid petitioning. This includes two distinct types of actions. A petitioner may be immune from the antitrust injuries which result from the petitioning itself. *See Noerr*, 365 U.S. at 143 (finding trucking industry plaintiffs' relationships with their customers and the public were hurt by the railroads' petitioning activities, yet the railroads were immune from liability). Also, and particularly relevant here, parties are immune from liability arising from the antitrust injuries caused by government action which results from the petitioning. *See Pennington*, 381 U.S. at 671 (holding plaintiffs could not recover damages resulting from the state's actions); *Mass. Sch. of Law at Andover, Inc. v. Am. Bar Assoc.*, 107 F.3d 1026, 1037 (3d Cir. 1997) (holding *Noerr* gave immunity for any damages stemming from state adoption of requirements for bar admission to petitioners who lobbied for their adoption); 1 Areeda & Hovenkamp, *supra*, at ¶ 202c. Therefore, if its conduct constitutes valid petitioning, the petitioner is immune from antitrust liability whether or not the injuries are caused by the act of petitioning or are caused by government action which results from the

petitioning. Here, we must determine whether a settlement agreement between private parties and sovereign states fits within the context of protected petitioning envisioned by the *Noerr-Pennington* doctrine.[30]

Finding that negotiating the settlement was akin to petitioning the government, the District Court held defendants immune under *Noerr-Pennington*. Specifically, it held that the "concerted effort by defendants to influence public officials, i.e., the states' Attorneys General, to accept a settlement in exchange for dismissing the numerous lawsuits pending against defendants is among the activities protected by the *Noerr-Pennington* doctrine." *A.D. Bedell*, 104 F.Supp.2d at 506. We agree that defendants engaged in petitioning activity with sovereign states and are immune under the *Noerr-Pennington* doctrine.[31]

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30. Despite plaintiffs' assertions, the Supreme Court has also made it clear that there is no "conspiracy" exception to *Noerr-Pennington* immunity. *See Omni*, 499 U.S. at 382 ("[W]e conclude that a 'conspiracy' exception to *Noerr* must be rejected."). Simply because the state officials might conspire with a private party to stifle competition does not mean that the action loses immunity. *See id.* 317 U.S. at 350-51 ("We find nothing in the language of the Sherman Act or in its history which suggests that its purpose was to restrain a state or its officers or agents from activities directed by its legislature.").

31. In doing so, we join other federal courts which have held the Multistate Settlement Agreement is entitled to *Noerr-Pennington* Immunity, though we recognize these cases did not involve identical facts. *See, e.g., Hise v. Philip Morris, Inc.*, 46 F.Supp.2d 1201, 1206 (N.D. Okla. 1999) (finding *Noerr-Pennington* immunity and not (Cont'd)

Appendix A

1.

The importance of the right to petition has been long recognized. As early as 1215, the Magna Carta granted barons the right to petition the King of England for redress. *See* Julie M. Spanbauer, *The First Amendment Right to Petition Government for a Redress of Grievances: Cut From a Different Cloth*, 21 Hastings Const. L.Q. 15, 17 (1993) (detailing history of the right to petition from 1215 through colonial times, the constitutional convention, and today). During our colonial period, the right to petition was widely used. The importance of this right was fundamental — it guaranteed not merely expression but the preservation of democracy.[32] "The very idea of government, republican in form, implies a right on the part of its citizens to meet peaceably for consultation in respect to public affairs and to petition for a redress of grievances." *United States v. Cruikshank*, 92 U.S. 542, 552 (1875).

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addressing *Parker* immunity), *aff'd mem.*, 208 F.3d 226 (10th Cir. 2000); *Forces Action Project LLC v. California*, No. C 99-0607 MJJ, 2000 WL 20977, at *8 (N.D. Cal. Jan. 5, 2000) (same); *PTI, Inc. v. Philip Morris, Inc.*, 100 F.Supp.2d 1179, 1193 (C.D. Cal. 2000) (finding *Noerr-Pennington* immunity and finding *Parker* immunity due to direct state action because "[t]he M.S.A. was negotiated by the states' attorneys general and approved by the state courts, and thus cannot be violative of the antitrust laws").

32. *See* Aaron R. Gary, *First Amendment Petition Clause Immunity From Tort Suits: In Search of A Consistent Doctrinal Framework*, 33 Idaho L. Rev. 67, 113-17 (1996) (discussing the importance of the freedom to petition beyond that of expression, in part because the Petitioning Clause guarantees access to elected representatives and directly promotes republican government).

Because of the importance of the right to petition the government freely, and because "[a]ntitrust law was . . . not intended to impose a barrier between the people and their government," *Noerr-Pennington* immunity extends beyond filing formal grievances directly with the government. *Balt. Scrap Corp. v. David J. Joseph Co.*, 237 F.3d 394, 398 (4th Cir. 2001) (holding secret funding of a lawsuit brought against a potential competitor to maintain a monopoly was protected under *Noerr-Pennington*, even though the funding party was not a litigant).

In a recent survey of the application of *Noerr-Pennington* immunity to non-traditional petitioning, *Primetime 24-Joint Venture v. Nat'l Broad. Co., Inc.*, 219 F.3d 92, 99-100 (2d Cir. 2000), the Court of Appeals for the Second Circuit noted the Supreme Court has extended *Noerr* immunity to actions before administrative agencies and the courts, *Cal. Motor Transp.*, 404 U.S. at 508, 510-11, and that other courts have extended *Noerr-Pennington* immunity to include efforts to influence governmental action incidental to litigation such as prelitigation threat letters. *McGuire Oil Co. v. Mapco., Inc.*, 958 F.2d 1552, 1560 (11th Cir. 1992); *Coastal States Mktg., Inc. v. Hunt*, 694 F.2d 1358, 1367-68 (5th Cir. 1983). There would seem to be no reason to differentiate settlement from other acts associated with litigation. *See Columbia Pictures Indus., Inc. v. Prof'l Real Estates Investors, Inc.*, 944 F.2d 1525, 1528-29 (9th Cir. 1991), *aff'd*, 508 U.S. 49 (1993) (affirming, but not addressing whether settlement creates immunity because sham exception defeated immunity). The Court of Appeals for the Seventh Circuit has recognized the application of *Noerr-Pennington* immunity to settlements between private parties and state

government. In *Campbell v. City of Chicago*, 823 F.2d 1182, 1186 (7th Cir. 1987), two cab companies were found immune from antitrust liability for their agreement to settle their lawsuits against the city in exchange for the passage of a favorable and arguably anticompetitive ordinance. The settlement in *Campbell* resonates favorably with the Multistate Settlement Agreement here.

The Supreme Court has yet to speak definitively on extending petitioning immunity to settlement agreements with sovereign states. Relying on a statement in *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*, plaintiffs claim the Supreme Court refused to extend immunity to settlement agreements when it stated that a "consent judgment, even one entered at the behest of the Antitrust Division, does not immunize the defendant from liability for actions, including those contemplated by the decree, that violates the rights of nonparties." 441 U.S. 1, 13 (1979). "But in any event, [we are] bound by holdings, not language." *Alexander v. Sandoval*, 531 U.S. 1049 (2001). We believe this case is easily distinguished. There was no settlement agreement in *Broadcast Music*. Rather, *Broadcast Music* involved actions taken years after the resolution of a claim by private actors who claimed they were acting under the protection of a consent decree. The Supreme Court ruled that the consent decree did not immunize the anticompetitive actions taken by private parties. For the above quoted language, *Broadcast Music* relied upon *Sam Fox Publishing Co. v. United States*, 366 U.S. 683, 689 (1961), which did not involve *Noerr-Pennington* immunity. *Sam Fox* addressed whether a non-participant is bound by the outcome of government antitrust litigation. *Id.* Neither *Broadcast Music*

nor *Sam Fox* mentioned *Noerr-Pennington* immunity, and neither is applicable to the facts here.

Plaintiffs claim a motivating purpose behind the Multistate Settlement Agreement was to create a cartel guaranteeing tobacco companies supracompetitive profits. Br. of Appellants at 49. Similarly, plaintiffs claim the States were motivated by a desire to share in these revenues. But the parties' motives are generally irrelevant and carry no legal significance.[33] *See Noerr*, 365 U.S. at 138. At the same time, it bears noting that the petitioning here invoked the States' traditional powers to regulate the health and welfare of its citizens. *See, e.g., Great Atlantic and Pac. Tea Co., Inc. v. Hugh B. Cottrell*, 424 U.S. 366, 370 (1976) ("[U]nder our constitutional scheme the States retain 'broad power' to legislate protection for their citizens in matters of local concern such as public health.").

In sum, we see no reason to distinguish between settlement agreements and other aspects of litigation between private actors and the government which give rise to antitrust immunity. The rationale is identical. Freedom from the threat

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33. Motive may be relevant if it demonstrates the party acted without a legitimate desire for government action, and desired to inflict harm only through petitioning, thus falling within the sham exception to *Noerr-Pennington* immunity. *See Noerr*, 365 U.S. at 138 (1961) (a party will not have immunity when petitioning activity "ostensibly directed toward influencing governmental action, is a mere sham to cover . . . an attempt to interfere directly with the business relationships of a competitor"). *See supra* note 29. Plaintiffs do not claim the defendants' conduct places them within the sham exception.

of antitrust liability should apply to settlement agreements as it does to other more traditional petitioning activities. We hold the defendants are immune under the *Noerr-Pennington* doctrine.

B. *Parker* Immunity

Having found the defendants immune under *Noerr-Pennington*, our analysis could end here. But the District Court found *Parker* immunity, so we will address it as well.

Antitrust laws do not bar anticompetitive restraints that sovereign states impose "as an act of government." *Parker v. Brown*, 317 U.S. 341, 352 (1943); *see also Mass. Sch. of Law at Andover, Inc. v. Am. Bar Assoc.*, 107 F.3d 1026, 1035 (3d Cir. 1997). The *Parker* doctrine relies heavily on the clarity of the State's goals and actions. "[S]tates must accept political responsibility for the actions they intend to undertake." *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621, 636 (1992). The key question is whether the allegedly anticompetitive restraint may be considered the product of sovereign state action. If it is not, then even if sectors of state government are involved, the activity will not constitute "state action" under the *Parker* doctrine and will not receive immunity.

"State action," as defined in cases granting *Parker* immunity, is qualitatively different from "state action" in other contexts such as the Fourteenth Amendment. *See* 1 Areeda & Hovenkamp, *supra*, at ¶ 221. While the Fourteenth Amendment can cover

> inadvertent or unilateral acts of state officials not acting pursuant to state policy . . . the term "state action" in antitrust adjudication refers only to government policies that are articulated with sufficient clarity that it can be said that these are in fact the state's policies, and not simply happenstance, mistakes, or acts reflecting the discretion of individual officials.[34]

Id. Because it is grounded in federalism and respect for state sovereignty, this interest in protecting the acts of the

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34. "State action" as defined by the *Parker* doctrine also differs from the government "actions" which results from petitioning discussed previously. *See supra*, Section III.A. The two are not coterminous. A finding of *Noerr-Pennington* immunity from injury caused by government action does not require a finding of *Parker* state action. *See* 1 Areeda & Hovenkamp, *supra*, at ¶ 206 (interpreting our dicta in *Massachusetts School of Law*, 107 F.3d 1026 (3d Cir. 1997) as noting this distinction). If the government "action" taken is the result of petitioning, *Noerr-Pennington* immunity attaches to a broader range of government action than does *Parker* immunity. *Noerr-Pennington* immunity protects petitioning, so long as it is not a sham. *See Subscription Television v. S. Cal. Theatre Owners Ass'n*, 576 F.2d 230, 233-34 (9th Cir. 1978) (holding defendants immune from antitrust liability under *Noerr-Pennington* even though their petitioning led to the passage of an unconstitutional initiative). Under *Noerr-Pennington* immunity, the government actions which flow from valid petitioning need not qualify as *Parker* "state action." Petitioning "would be considerably chilled by a rule which would require an advocate to predict whether the desired legislation would withstand a constitutional challenge in the courts and to expose itself to a potential treble antitrust action based on that prediction." *Subscription Television*, 576 F.2d at 233.

sovereign state, even if anticompetitive, outweighs the importance of a freely competitive marketplace, especially in the absence of contrary congressional intent.

Without clear congressional intent to preempt, federal laws should not invalidate state programs. "In a dual system of government in which, under the Constitution, the states are sovereign, save only as Congress may constitutionally subtract from their authority, an unexpressed purpose to nullify a state's control over its officers and agents is not lightly to be attributed to Congress." *Parker v. Brown*, 317 U.S. 341, 351 (1943). While individual anticompetitive acts of state governments may be considered unwise or counterproductive, the decision to make such choices lies within the sovereign power of the states. Congress did not intend to override important state interests in passing the Sherman Act. "The general language of the Sherman Act should not be interpreted to prohibit anticompetitive actions by the States in their governmental capacities as sovereign regulators." *City of Columbia v. Omni Outdoor Adver.*, 499 U.S. 365, 374 (1991).

The Sherman Act was enacted to address the unlawful combination of private businesses. *See Apex Hosiery Co. v. Leader*, 310 U.S. 469, 493 n.15 (1940) ("The history of the Sherman Act as contained in the legislative proceedings is emphatic in its support for the conclusion that 'business competition' was the problem considered and that the act was designed to prevent restraints of trade which had a significant effect on such competition."). "There is no suggestion of a purpose to restrain state action in the Act's legislative history." *Parker*, 317 U.S. at 343. The Sherman

Act was passed "in the era of 'trusts' and of 'combinations' of businesses and of capital organized and directed to control of the market by suppression of competition in the marketing of goods and services, the monopolistic tendency of which had become a matter of public concern." *Apex*, 310 U.S. at 493. Given its focus on the problems of private monopolies and combinations, it is not surprising that the Sherman Act does not set out to curb clearly defined anticompetitive state actions. *See Cal. Retail Liquor Dealers Assoc. v. Midcal Aluminum, Inc.*, 445 U.S. 97, 104 (1980).

When a state clearly acts in its sovereign capacity it avoids the constraints of the Sherman Act and may act anticompetitively to further other policy goals. *See S. Motor Carriers Rate Conference, Inc. v. United States*, 471 U.S. 48, 54 (1985). For example, state governments frequently sanction monopolies to ensure consistent provision of essential services like electric power, gas, cable television, or local telephone service. But "a state does not give immunity to those who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful." *Parker*, 317 U.S. at 351 (states cannot authorize private parties to set a price and then enforce those prices without any evaluation of their reasonableness). Only an affirmative decision by the state itself, acting in its sovereign capacity, and with active supervision, can immunize otherwise anticompetitive activity.

When it is uncertain whether an act should be treated as state action for the purposes of *Parker* immunity, we apply the test set forth in *California Retail Liquor Dealers Association v. Midcal Aluminum, Inc.*, 445 U.S. 97, 104

(1980), to "determine whether anticompetitive conduct engaged in by private parties should be deemed state action and thus shielded from the antitrust laws." *Patrick v. Burget*, 486 U.S. 94, 100 (1988). Applying *Midcal* is unnecessary if the alleged antitrust injury was the *direct result* of a clear sovereign state act. *Mass. Sch. of Law at Andover v. Am. Bar Assoc.*, 107 F.3d 1026, 1036 (3d Cir. 1997); *Sessions Tank Liners, Inc. v. Joor Mfg., Inc.*, 17 F.3d 295, 299 (9th Cir. 1994) (finding immunity from antitrust liability where "injuries for which [the plaintiff] seeks recovery flowed directly from government action"). In *Massachusetts School of Law*, we held that where "the states are sovereign in imposing the bar admission requirements [the alleged anticompetitive restraints], the clear articulation and active supervision requirements . . . are inapplicable." 107 F.3d at 1036. There is less need for scrutiny "[w]hen the conduct is that of the sovereign itself . . . [because] the danger of unauthorized restraint of trade does not arise." *PTI, Inc. v. Philip Morris, Inc.*, 100 F.Supp.2d 1179, 1196 (C.D. Ca. 2000). Similarly, concerns about the legitimacy of the action are reduced. Thus we must first decide if *Midcal* applies to the States' actions in negotiating and implementing the Multistate Settlement Agreement.

The Supreme Court has recognized state legislative and judicial action as sovereign under *Parker*. But "[c]loser analysis is required" when the action is less directly that of the legislature or judiciary. *Hoover v. Ronwin*, 466 U.S. 558, 568 (1984) (relying in part on *Midcal*). One Court of Appeals has decided that executive officers and agencies "are entitled to *Parker* immunity for actions taken pursuant to their constitutional or statutory authority, regardless whether these

particular actions or their anticompetitive effects were contemplated by the legislature," without the need for *Midcal* analysis. *Charley's Taxi Radio Dispatch Corp. v. SIDA of Haw., Inc.*, 810 F.2d 869, 876 (9th Cir. 1987). We have yet to address whether the acts of executive officials constitute state action that avoids *Midcal* analysis. Furthermore, in this case, we must determine whether the antitrust injuries were more attributable to private parties than to government action, as was the case in *Midcal*.[35]

1. Direct Application of *Parker*

An argument can be made that the Multistate Settlement Agreement, and any of its anticompetitive effects, were the

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35. *Parker*, by its own terms, immunizes only states. But in order to give *effect* to *Parker* immunity, private parties to state action must also be immune. *Armstrong Surgical Ctr, Inc. v. Armstrong County Mem'l Hosp.*, 185 F.3d 154, 159 (3d Cir. 1999) ("[I]f relief is sought solely for injury as to which the state would enjoy immunity under *Parker*, the private petitioner also enjoys immunity."). Otherwise, plaintiffs could sue only the private parties and by winning antitrust judgments against them, could thwart state policies as if there were no state immunity. No state could enter into an agreement with private groups, even to further clear state policies, because the potential liability of the private groups would prevent them from joining. Artful pleading should not frustrate state policy. *S. Motor Carriers Rate Conference, Inc., v. United States*, 471 U.S. 48, 56-57 (1985) (absent immunity for private parties, a "plaintiff could frustrate any State program merely by filing suit against the regulated private parties"). If *Parker* immunity attaches, it would also reach the private participants of the Multistate Settlement Agreement.

direct result of state government action.[36] For each signatory state, there was active involvement by high ranking executive officials and the agreement was subject to state court approval. The Multistate Settlement Agreement was negotiated by Attorneys General from each state to settle existing and contemplated lawsuits. The Multistate Settlement Agreement required that,

> each Settling State that is a party to a lawsuit . . . and each Participating Manufacturer will:
>
> > (A) tender this agreement to the Court in such Settling State for its approval; and

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36. The District Court found direct state action and thus did not apply *Midcal. A.D. Bedell*, 104 F.Supp.2d at 507 ("After careful consideration of the submissions of the parties and the amici curiae, I conclude that because the conduct of entering into, executing and implementing the M.S.A. was undertaken by the settling states functioning in their sovereign capacities, to the extent Plaintiff's injuries are premised upon said conduct, liability for said conduct by the states would be subject to *Parker* state action immunity. Obviously in so holding, I opine, contrary to the argument presented by Plaintiff, that in this case, application of the *Cal. Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980), test is inappropriate."). Similarly, one other court which has addressed the Multistate Settlement Agreement has found the presence of direct state action and did not undertake a *Midcal* analysis. *See PTI, Inc. v. Philip Morris, Inc.*, 100 F.Supp.2d 1179, 1196 (C.D. Cal. 2000) (finding that because of the direct actions by the State Attorneys General, approval by state courts, and implementation of Qualifying Statutes by state legislatures, the Multistate Settlement Agreement was the result of direct state action, rendering *Midcal* inapplicable).

> (B) tender to the Court in such Settling state for entry of a consent decree conforming to the model consent decree attached hereto as Exhibit L.

MSA § XIII(b)(1); *see also PTI*, 100 F.Supp.2d at 1196.

In most cases, the state legislatures were involved as well. Although they lacked a direct role in forming or approving the Multistate Settlement Agreement, the legislatures were charged with, and responsible for, the enactment of the Qualifying Statutes which, although technically voluntary, enforce important components of the Multistate Settlement Agreement. *See* MSA § IX(d)(2)(E), (F) and (G). It is apparent that legislative enactment of the Qualifying Statutes signified state approval of the Multistate Settlement Agreement. *See Cal. Aviation Inc. v. City of Santa Monica*, 806 F.2d 905, 909 n.5 (9th Cir. 1986) (noting statutes passed afterwards can be evidence of pre-existing state policy to allow anticompetitive behavior). In a few states, the legislatures played an even greater role by applying pressure on the Attorney General or Governor to bring suit or by passing legislation authorizing the Attorney General to bring suit against the tobacco companies.[37] Additionally,

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37. *See* Kris Mayes, *Legislators Say States Should Sue Tobacco Firms*, The Arizona Republic, March 23, 1996, at B1 (reporting state lawmakers in Arizona urged the State Attorney General to join other states and file suit); Ron Scherer, *More States Plan to Sue for Costs of Smoking*, The Christian Science Monitor, July 12, 1994, at 6 (stating the Florida and Massachusetts legislatures passed bills that permitted the states to sue the tobacco companies for reimbursement of medical expenses).

each branch of state government had a role in the execution or operation of the Multistate Settlement Agreement. Under this analysis, one could find direct state action foreclosing the application of *Midcal.*

Under a different view, we focus not on the negotiation and consummation of the Multistate Settlement Agreement, but on its actual *operation* and resulting effects, since that is the true cause of the anticompetitive effects. This is how the Supreme Court analyzed the behavior in *Midcal.*

In *Midcal*, the price setting structure that resulted in antitrust injury would not have existed but for the state regulation. Only because of state legislative enactments did California wine producers hold power over the wholesalers to engage in resale price maintenance. *Midcal*, 445 U.S. at 105. Because the actual parties involved in the anticompetitive behavior were private parties, the Supreme Court determined the alleged violation of the antitrust laws was not obvious state action and devised what has come to be known as the *Midcal* test.

We have found direct state action, without *Midcal* analysis, only when the allegedly anticompetitive behavior was the direct result of acts within the traditional sovereign powers of the state. *See Mass. Sch. of Law*, 107 F.3d at 1036; *see also Zimomra v. Alamo Rent-A-Car, Inc.*, 111 F.3d 1495, 1500 (10th Cir. 1997). In *Massachusetts School of Law*, we held *Midcal* inapplicable because the state acted as sovereign in imposing bar admission requirements. 107 F.3d at 1036 (Massachusetts School of Law at Andover, Inc., an unaccredited law school, had challenged the state

requirement that a student graduate from an ABA accredited law school as an anticompetitive restraint). We distinguished *Midcal* and its progeny as "inapplicable because they dealt with situations where private parties were engaging in conduct . . . which led directly to the alleged antitrust injury." *Id.* Similarly, in *Zimomra*, the Court of Appeals for the Tenth Circuit held *Midcal* inapplicable in a challenge to rental car price fixing because the city and county, and not a private actor, had the ultimate responsibility for setting rental car daily use fees and the private parties "had no such discretionary authority." 111 F.3d at 1500. In neither case was a private party responsible for the resulting anticompetitive act; and thus there was no need to apply the *Midcal* analysis.

Although the Multistate Settlement Agreement was a negotiated settlement by State Attorneys General, and the state legislatures were responsible for passing the Qualifying Statutes to enforce important components of the agreement, these acts by the governmental parties were not the direct source of the anticompetitive injuries.[38] Therefore, it would appear that, just as the injury in *Midcal* was caused by private parties taking advantage of the state imposed market structure, the anticompetitive injury here resulted from the tobacco companies' conduct after implementation of the Multistate Settlement Agreement, and not from any further positive action by the States. Even though, as defendants argue, the Multistate Settlement Agreement created the cartel, this fact makes the case analogous to *Midcal*, not different.

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38. The defendants claim any injury here occurs because of the these acts and not because of private action. Br. of Appellees at 31.

The signing of the Multistate Settlement Agreement and the establishment of the output cartel are not purely private actions, nor are they entirely attributable to the state in the manner of a legislative act. As such, this case resembles a "hybrid restraint" as discussed by Justice Stevens in his concurrence in *Rice v. Norman Williams Co.*, 458 U.S. 654, 666-67 (1982) (Stevens, J., concurring).[39] Hybrid restraints are not the type of sovereign state action found in *Massachusetts School of Law* or *Zimomra*, that avoid *Midcal* treatment. Instead, hybrid restraints involve a degree of private action which calls for *Midcal* analysis. *See Rice*, 458 U.S. at 666 ("Hybrid restraints of this character require analysis that is different from a public regulatory scheme on the one hand, and a purely private restraint on the other.") (citations omitted) (Stevens, J., concurring). Therefore, to determine if the allegedly anticompetitive sections of the Multistate Settlement Agreement were "state action" under the *Parker* doctrine, we will apply the *Midcal* analysis.

For the reasons expressed, namely that the antitrust injuries here were not caused by the solitary acts of the state acting in its traditional capacity, but were instead caused by hybrid acts involving private parties in the unique setting of a joint settlement, we believe this form of alleged anticompetitive restraint requires the *Midcal* analysis.

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39. The Supreme Court has "twice held that hybrid price-fixing restraints are prohibited by the Sherman Act." *Id.* "In both cases the private decision to fix prices was unsupervised by the State but made effective by state law." *Rice*, 458 U.S. at 666 (Stevens, J., concurring) (citing *Schwegmann Bros. v. Calvert Distillers Corp.*, 341 U.S. 384 (1951); *Midcal*, 445 U.S. 97).

2. *Midcal*

To qualify as state action under the *Midcal* test, "the challenged restraint must be one 'clearly articulated and affirmatively expressed as state policy.' " 445 U.S. at 104 (quoting *City of Lafayette v. La. Power & Light Co.*, 435 U.S. 389, 410 (1978) (opinion of Brennan, J.)). A government entity need not "be able to point to a specific, detailed, legislative authorization" to assert a successful *Parker* defense. *Lafayette*, 435 U.S. at 415. But it must be evident that under the "clear articulation" standard the challenged restraint is part of state policy. As the Supreme Court has stated, "*Midcal* confirms that while a State may not confer antitrust immunity on private persons by fiat, it may displace competition with active state supervision if the displacement is both intended by the State and implemented in its specific details." *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621, 633 (1992).

Here, the States' reasons for bringing suits against the Majors — to reduce teenage smoking, address public health concerns, and recoup state health care expenditures — were evident and clearly articulated. State Attorneys General and Governors made public pronouncements which received national coverage.[40] Other suing states made similar

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40. *See, e.g., Maryland Seeks Billions From Tobacco Firms for Medicaid Costs*, Washington Post, May 2, 1996, at B5 (quoting Maryland Attorney General Joseph Curran's press conference where he stated, "[The tobacco companies] have knowingly peddled a killer product, and their victims come to hospitals just like this to be treated and to die. Now we will take them to a courthouse to seek justice

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announcements and cited to studies demonstrating the enormous impact of cigarette smoking on health and finances.[41] The proclaimed goals of the States were clear.

As noted, the State Attorneys General and the Governors were not the only state actors involved. The State Attorneys General took the lead in negotiations, but the state courts played an important role in approving the Multistate

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for their deceitful conduct."); Kendrick Blackwood, *Iowa Sues Over Costs of Smoking; 22 Tobacco Groups Named Defendants*, Omaha World Herald, Nov. 27, 1996, at 1 (quoting Iowa Governor Terry Branstad announcing the decision to bring suit and stating, "For too long, taxpayers have footed the bill for the immense strain that smoking has caused on our health-care system. With this suit, we are seeking justice.").

41. *See, e.g.*, *Oklahoma Sues Tobacco Industry for Over $1 Billion; State Seeks Medicaid Funds on Smoke-Related Interests*, The Baltimore Sun, Aug. 23, 1996, at C2 (quoting Oklahoma Attorney General Drew Edmondson's statement that "Oklahoma has spent about $70 million a year in Medicaid contributions since 1980 to treat patients with smoking-related illnesses"); Kevin McDermott, *Illinois to Sue Tobacco Firms; State Seeks to Recover Medicaid Expenditures*, St. Louis Post-Dispatch, Sept. 18, 1996, at A1 (reporting that Illinois Attorney General Jim Ryan's office estimates that Illinois spent $2.75 billion in Medicaid to treat smoking related illnesses between 1980 and 1993); Amy Goldstein, *Maryland to Sue Makers of Cigarettes: Effect of Smoking on Medicaid at Issue*, Washington Post, Nov. 17, 1995, at B1 (quoting a state study referred to by the Attorney General and Governor of Maryland in support of their decision to sue the tobacco companies which concluded that 40% of cancer deaths in Maryland were cancers often caused by smoking).

Settlement Agreement by issuing consent judgments and dismissing the lawsuits. This was required by the Multistate Settlement Agreement which provided that each signatory state would "tender to the Court in such Settling State for entry of a consent decree conforming to the model consent decree" included in the agreement. *See* MSA § XIII(b)(1). The lawsuits were dismissed under the consent agreements. The state legislatures also demonstrated their approval in most of the States by passing implementing legislation. *See Cal. Aviation Inc.*, 806 F.2d at 909 n.5 (noting that statutes passed afterwards are evidence of pre-existing state policy to allow anticompetitive behavior). Even before the settlement, legislatures of some states targeted the tobacco industry by putting pressure on the Attorney General or Governor to bring suit.[42] In view of public pronouncements of the States' intentions and goals, along with active involvement from each branch of state government, it is evident the Multistate Settlement Agreement was backed by clearly articulated state policy.[43]

The second prong of the *Midcal* test is whether the resulting antitrust violation was "actively supervised" by the state. This standard is more problematic. The essential

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42. *See, e.g.*, Kris Mayes, *Legislators Say State Should Sue Tobacco Firms*, The Arizona Republic, March 23, 1996, at B1 (reporting state lawmakers in Arizona urged the state Attorney General to join other states and file suit); Ron Scherer, *More States Plan to Sue for Costs of Smoking*, The Christian Science Monitor, July 12, 1994, at 6.

43. We do not hold that public pronouncement through the media is necessarily required to satisfy the clear articulation prong.

inquiry of the "actively supervised" prong is to determine if the "anticompetitive scheme is the State's own." *FTC v. Ticor Title Ins. Co.*, 504 U.S. 621, 635 (1992). The active supervision prong "requires that state officials have and exercise power to review particular anticompetitive acts of private parties and disapprove those that fail to accord with state policy." *Patrick v. Burget*, 486 U.S. 94, 101 (1988). "Absent such a program of supervision, there is no realistic assurance that a private party's anticompetitive conduct promotes state policy, rather than merely the party's individual interests." *Id.* at 100-01. "Such active state review is clearly necessary where private defendants are empowered with some type of discretionary authority in connection with the anticompetitive acts (e.g. to determine price or rate structures)." *Zimomra*, 111 F.3d at 1500. Rubber stamp approval of private action does not constitute state action. A state must independently review and approve the anticompetitive behavior to satisfy this prong of the *Parker* doctrine. *Patrick*, 486 U.S. at 101 ("The active supervision requirement mandates that the State exercise ultimate control over the challenged anticompetitive conduct."); *Ticor*, 998 F.2d at 1139.

Here, plaintiffs allege the Multistate Settlement Agreement primarily furthers the private tobacco companies' interests and not those of the States. While we do not agree with this characterization, it is clear the Multistate Settlement Agreement empowers the tobacco companies to make anticompetitive decisions with no regulatory oversight by the States. Specifically, the defendants are free to fix and raise prices, allegedly without fear of competition. The question then is whether the Multistate Settlement

Agreement, with all its duties and responsibilities, creates sufficient state supervision even though the pricing decisions are unregulated.

The States actively and continually monitor the implementation of portions of the Multistate Settlement Agreement. *See* MSA §§ VII-VIII. After requiring a state court consent decree, the Multistate Settlement Agreement also mandates state courts to maintain continuing jurisdiction over enforcement of disputes between the States and the tobacco companies. *See* MSA § VII(a). Under the Multistate Settlement Agreement, the state courts may order compliance in the form of an Enforcement Order. *See* MSA § VII(c)(3). If a State Attorney General believes a manufacturer has failed to comply with an Enforcement Order, it may seek an order for civil contempt or monetary sanction to force compliance. *See* MSA § VII(c)(4). Furthermore, for a period of seven years after settlement, the Attorney General of a Settling State may inspect all non-privileged records of the tobacco companies, and will have access to interview directors, officers and employees upon reasonable belief of a violation of the Multistate Settlement Agreement. *See* MSA § VII(g).

The Multistate Settlement Agreement also establishes a $50 million fund to assist the States in enforcing the Multistate Settlement Agreement. *See* MSA § VIII(c). This fund is to be used

> to supplement the States'
>
> > (1) enforcement and implementation of the terms of [the Multistate Settlement Agreement] and consent decrees, and

> (2) investigation and litigation of potential violations of laws with respect to Tobacco Products.

Id. This includes prosecution of non-signatories for those underlying "torts" which initially led the States to sue the major tobacco companies.[44]

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44. The Multistate Settlement Agreement also creates administrative obligations. The Multistate Settlement Agreement provides:

> VIII. CERTAIN ONGOING RESPONSIBILITIES OF THE SETTLING STATES
>
> (a) Upon approval of the NAAG [National Association of Attorneys General] executive committee. NAAG will provide coordination and facilitation for the implementation and enforcement of this Agreement on behalf of the Attorneys General of the Settling States, including the following:
>
> (1) NAAG will assist in coordinating and Inspection and discovery activities referred to in subsections III(p)(3) and VII(g) regarding compliance with this Agreement by the Participating Manufacturers and any new tobacco-related trade associations.
>
> (2) NAAG will convene at least two meetings per year and one major national conference every three years for the Attorneys General of the Settling States, the directions of the Foundation and three

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Appendix A

The largest responsibilities for the tobacco companies are financial. The Multistate Settlement Agreement details how and when the payments will be made to the settling states each year. *See* MSA § IX.[45] In addition, there is a

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> persons designated by each Participating Manufacturer. The purpose of the meetings and conference is to evaluate the success of this Agreement and coordinate efforts by the Attorneys General and the Participating Manufacturers to continue to reduce Youth Smoking.
>
> (3) NAAG will periodically inform NGA, NCSL, the National Association of Counties and the National League of Cities of the results of the meetings and conferences referred to in subsection (a)(2) above.
>
> (4) NAAG will support and coordinate the efforts of the Attorneys General of the Settling States in carrying out their responsibilities under this Agreement.
>
> (5) NAAG will perform the other functions specified for it In this Agreement, including the functions specified in section IV.

MSA § VIII(a).

45. In pertinent part, payments are calculated as follows:

> (c) Annual Payments and Strategic Contribution Payments

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Appendix A

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(1) On April 15, 2000 and on April 15 of each year thereafter in perpetuity, each Original Participating Manufacturer shall severally pay to the Escrow Agent (to be credited to the Subsection IX(c)(1) Account) its Relative Market Share of the base amounts specified below, as such payments are modified in accordance with this subsection (c)(1):

Year	Base Amount
2000	$4,500,000,000
2001	$5,000,000,000
2002	$6,500,000,000
2003	$6,500,000,000
2004	$8,000,000,000
2005	$8,000,000,000
2006	$8,000,000,000
2007	$8,000,000,000
2008	$8,139,000,000
2009	$8,139,000,000
2010	$8,139,000,000
2011	$8,139,000,000
2012	$8,139,000,000
2013	$8,139,000,000
2014	$8,139,000,000
2015	$8,139,000,000
2016	$8,139,000,000
2017	$8,139,000,000
2018 and each year thereafter	$9,000,000,000

The Payments made by the Original Participating Manufacturers pursuant to this

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limited "most-favored nation" provision. In the event a State settles with a non-signatory tobacco company (NPM) on terms more favorable than the Multistate Settlement Agreement (a lower payment-per-pack amount), then all signatories will be entitled to a revision of the Multistate Settlement Agreement to at least match the new agreement. *See* MSA § XVIII(b)(2).[46] There are also significant ongoing

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> subsection (c)(1) shall be subject to the Inflation Adjustment, the Volume Adjustment, the Previously Settled States Reduction, the Non-Settling States Reduction, the NPM Adjustment, the offset for miscalculated or disputed payments described in Section XI(i), the Federal Tobacco Legislation Onset, the Litigating Release Parties Offset, and the offsets for claims over described in subsections XII(a)(4)(B) and XII(a)(8).

MSA § IX(c)(1).

46. The "most-favored nations" clause provides:

> If any Settling State resolves by settlement Claims against any Non-Participating Manufacturer after the MSA Execution Date comparable to any Released Claim, and such resolution includes overall terms that are more favorable to such Non-Participating Manufacturers than the terms of this Agreement (including, without limitation, any terms that related to the marketing or distribution of Tobacco Products and any term that provides for a lower settlement cost on a

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restrictions placed on the tobacco manufacturers. They are prohibited from taking "any action, directly or indirectly, to target Youth within any Settling State in the advertising, promotion, or marketing of Tobacco Products," MSA § III(a); they also agreed to refrain from using "any cartoon in the advertising, promoting, packaging or labeling of Tobacco products." MSA § III(b).

Despite these factors, we are not convinced that the States satisfy *Midcal*'s "active supervision" prong. This is because the States' supervision does not reach the parts of the Multistate Settlement Agreement that are the source of the antitrust injury. It is the conduct that violates the antitrust laws that states must "actively supervise" in order for *Parker* immunity to attach.

As we recognized in *Norman's on the Waterfront, Inc. v. Wheatley*, "an arrangement sponsored by the state is not necessarily state action for the purposes of the antitrust laws." 444 F.2d 1011, 1017 (3d Cir. 1971) (citing *Woods Exploration & Producing Co., Inc. v. Aluminum Co. of Am.*, 438 F.2d

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> per pack sold basis), then the overall terms of this Agreement will be revised so that the Original Participating Manufacturers will obtain, with respect to that Settling State, overall terms at least as relatively favorable (taking into account, among other things, all payments previously made by the Original Participating Manufacturers and the timing of any payments) as those obtained by such Non-Participating Manufacturers pursuant to such resolution of claims . . . .

MSA § XVIII(b)(2).

1286, 1294 (5th Cir. 1971) for the proposition that "it is not every governmental act that points a path to an antitrust shelter"). In *Wheatley*, we analyzed a series of *Parker* cases demonstrating the state must be actively involved in establishing the rules of the market as well as in the anticompetitive activity. Because " 'states can neither authorize individuals to perform acts which violate the antitrust laws nor declare that such action is lawful,' " many of these cases of hybrid restraints turn on whether the state remains involved in the actual pricing by the regulated parties. *Wheatley*, 444 F.2d at 1017 (quoting *Asheville Tobacco Bd. of Trade, Inc. v. Fed. Trade Comm'n*, 263 F.2d 502, 509 (4th Cir. 1959)).

Significantly, in *Midcal*, the State of California enacted a pricing system for the wine industry. Because the State did not exercise direct control over the resulting prices set by the private actors, and did not review the reasonableness of the prices, the Supreme Court found insufficient "active supervision" to qualify as state action. *Midcal*, 445 U.S. at 105-06. Therefore, there was no immunity for setting anticompetitive prices under this system. *Id.*

In *Midcal*, the challenged "restraints" were state statutes on pricing and resale price maintenance. But there were several other ways in which the State of California regulated the wine industry. *See, e.g.*, Cal. Bus & Prof. Stat. Ann. §§ 25600-67 (West 1964).[47] California actively supervised

47. Although some of these statutory provisions have been amended since *Midcal*, the bulk were enacted before *Midcal* (in 1953). Here we cite the statutes as they existed when *Midcal* was decided.

when, where, and to whom wine or other alcoholic beverages could be sold,[48] the markings and signs on labels,[49] penalties for underage use,[50] and advertisements, including prohibiting advertising to minors.[51] This "supervision" was not cited in *Midcal* because it did not constitute part of the anticompetitive restraint at issue. Under *Parker*, a comprehensive regulatory scheme would be immune from antitrust liability because the "State would 'displace unfettered business freedom' with its own power," *Midcal*, 445 U.S. at 106. But the Supreme Court in *Midcal* was silent about the impact of other regulatory provisions in the California Code denoting, we believe, the absence of a comprehensive regulatory scheme in this sense.

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48. Cal. Bus & Prof. Stat. Ann. § 25602 (West 1964) (prohibiting sales to an intoxicated person); Cal. Bus & Prof. Stat. Ann. § 25607 (prohibiting the sale of alcohol without a license for the specific alcohol); Cal. Bus & Prof. Stat. Ann. § 25608 (prohibiting possession, consumption or sale of alcohol on school property); Cal. Bus & Prof. Stat. Ann. § 25631 (prohibiting the sale of alcoholic beverages between 2 a.m. and 6 a.m.).

49. Cal. Bus & Prof. Stat. Ann. § 25610 (prohibiting the destruction of labels whose presence is required by federal or state law).

50. Cal. Bus & Prof. Stat. Ann. § 25658 (prohibiting consumption or purchase of alcohol by a minor).

51. Cal. Bus & Prof. Stat. Ann. § 25611 (restricting the size of signs advertising alcoholic beverages); Cal. Bus & Prof. Stat. Ann. § 25612 (prohibiting "obnoxious, gaudy, blatant, or offensive" alcohol advertisements); Cal. Bus & Prof. Stat. Ann. § 25664 (prohibiting the use of any advertisement intended to encourage minors to drink).

Appendix A

Since *Midcal*, other courts have found that if a state creates or sanctions a monopoly or cartel through its sovereign powers, but does not regulate the resulting prices, the resulting anticompetitive behavior should not be granted immunity. In *Wheatley*, we held that because the Virgin Islands Alcoholic Beverages Fair Trade Law did not grant the power to "approve, disapprove, or modify the prices fixed by private persons," the program could not meet the active supervision prong of *Midcal* and was not immune under *Parker*. In *Asheville Tobacco*, the Court of Appeals for the Fourth Circuit held that where a state statute authorized the creation of local tobacco boards to regulate tobacco sales at auctions, and where the states did not continue to supervise the decisions of these boards, the board's actions were not protected by *Parker* immunity. This principle has also been applied in state granted monopoly cases. In *Gas Light Co. of Columbus v. Georgia Power Co.*, 440 F.2d 1135 (5th Cir. 1971), the Court of Appeals for the Fifth Circuit found a utility which had been given a monopoly by the state was entitled to *Parker* immunity only because its prices were regulated extensively by the state through a process of full adversarial hearings.

In each of these cases, the decision by the state to allow, or even to create, an anticompetitive scheme did not establish immunity. As a leading antitrust treatise has recognized, "A state may be free to determine for itself how much competition is desirable, provided that it substitutes adequate control wherever it has substantially weakened competition." Areeda & Hovenkamp, *supra*, at ¶ 221 (citing *Wheatley*, *Asheville Tobacco*, and *Georgia Power*). Under this jurisprudence, only when the state approves and actively

supervises the results of the anticompetitive scheme does *Parker* immunity attach.

As noted, some provisions of the Multistate Settlement Agreement actively regulate the tobacco companies, like those imposing advertising restrictions.[52] But these provisions have no effect on pricing or production and thus do not regulate the challenged anticompetitive conduct. *Patrick*, 486 U.S. at 101. In contrast, the anticompetitive restraints in the Multistate Settlement Agreement that permit the tobacco companies to maintain an output cartel are the Renegade Clause and, arguably, the resulting Qualifying Statutes.

The States here are actively involved in the maintenance of the scheme, but they lack oversight or authority over the tobacco manufacturers' prices and production levels. These decisions are left entirely to the private actors. Nothing in the Multistate Settlement Agreement or its Qualifying Statutes gives the States authority to object if the tobacco companies raise their prices. In fact, it appears these increases have already happened. As noted, the Majors have raised their prices sharply and uniformly since the implementation of the Multistate Settlement Agreement — according to plaintiffs, by 50% since 1997. *See* Complaint at ¶ 36. These price increases have not been monitored or regulated by the States. The Multistate Settlement Agreement imposes no restrictions on pricing or provisions to temper the effects of

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52. *See* MSA § III (restricting the targeting of youth, the use of cartoons, and imposing other wide reaching regulations on advertising).

the output cartel.[53] Under this set of facts, there is insufficient evidence of active supervision of the allegedly anticompetitive restraints to satisfy this prong of *Midcal*.[54]

Although the Multistate Settlement Agreement is the product of a "clearly articulated" state policy, because the States do not "actively supervise" the *anticompetitive restraints*, the participants are not entitled to *Parker* immunity.[55]

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53. We could speculate that this prong might be met if there were provisions in the Multistate Settlement Agreement which granted the state oversight authority on the reasonableness of price increases. It is also the case that under certain circumstances, immunity may attach even in the absence of supervision where the state action creates a scheme where anticompetitive behavior is certain to occur and where further supervision would serve no purpose. *See* 1 Areeda & Hovenkamp, *supra*, at ¶ 221e4, ¶ 226e (citing examples). However, in this case, the Multistate Settlement Agreement left significant decisions to private decision makers. The actual pricing decisions are exclusively under the control of the tobacco companies. Only their effects are governed by the structure of the Multistate Settlement Agreement.

54. An argument could be made that the Multistate Settlement Agreement cannot be parsed into anticompetitive restraints and non-anticompetitive restraints. But the better argument appears to be that restrictions on advertising and the like cannot save a pricing system or output control system that is not actively supervised — even if those regulations are within the same document (like the Multistate Settlement Agreement) or are located within the same statutory code (as in *Midcal*). That other restrictions on wine distribution and consumption and other supervision of the wine industry are not discussed in *Midcal* supports this conclusion.

55. Plaintiffs assert that even if we were to find *Parker* immunity, there is a conspiracy exception, and that the defendants

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here fall within that exception. There is also a market participant exception to actions which might otherwise be entitled to *Parker* immunity. The District Court addressed neither argument but on appeal both parties briefed these issues. Although we do not find *Parker* immunity, we find it useful to clarify these exceptions.

At one point, several courts of appeals had opined that the language in *Parker* which discusses the market participant exception, created a broad conspiracy exception. *See City of Columbia v. Omni Outdoor Adver., Inc.*, 499 U.S. 365, 374 (1991). The Court in *Parker* stated, "We have no question of the state or its municipality becoming a participant in the private agreement or combination by others for restraint of trade." 317 U.S. at 351-52 (citing *Union Pac. R. Co. v. United States*, 313 U.S. 450 (1941)). The reading of a conspiracy exception also based on language in *Parker* which said, "The state in adopting and enforcing the prorate program made no contract or agreement and entered into no conspiracy in restraint of trade or to establish monopoly but, as sovereign, imposed the restraint as an act of government which the Sherman Act did not undertake to prohibit." *Id.* at 352. But just as under *Noerr-Pennington* immunity, the state does not forfeit *Parker* immunity simply because it acts with a private party. In *Omni*, the Supreme Court made it clear that "[t]here is no such conspiracy exception." *Id.* The Court has clarified that the language in *Parker* meant "immunity does not necessarily obtain where the State acts not in a regulatory capacity but as a commercial participant in a given market." *Id.*

As an example of what it means to be a commercial or market participant, the Court in *Omni* cites *Union Pac. R. Co. v. United States*, 313 U.S. 450 (1941), in which the City of Kansas City was held liable for certain "rebates and concessions made . . . in its capacity as the owner and operator of a wholesale produce market that was integrated with railroad facilities." *Id.* at 375.
(Cont'd)

3.

The question of *Parker* immunity's applicability is a difficult one. As noted, we hold we must apply the *Midcal*

(Cont'd)
The government entity therefore was involved in the market as a buyer or seller. Other than *Union Pacific*, there has been little elaboration about the commercial participant exception to *Parker* immunity.

The commercial or market participant exception, however, is a concept made familiar by Dormant Commerce Clause jurisprudence. State actions are immune from the Dormant Commerce Clause when they are regulatory actions but not where the state acts as a market participant — just as in Sherman Act antitrust cases. *See New Energy Co. v. Limbach*, 486 U.S. 269, 277 (1988) ("[The market participant exception] differentiates between a State's acting in its distinctive governmental capacity, and a State's acting in the more general capacity of a market participant; only the former is subject to the limitations of the negative Commerce Clause."). Dormant Commerce Clause cases have found the market participant exception appropriate where the state action "constituted a direct state participation in the market." *Camps Newfound/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564, 593 (1997). This includes a state program to pay people who remove abandoned cars from streets and junkyards because the payment was interpreted as an entry into the market for abandoned cars, *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794, 810 (1976); a program to sell output from a state owned and operated cement plant, *Reeves, Inc. v. Stake*, 447 U.S. 429, 431-32 (1980); and a program to fund construction projects entirely by a city. *White v. Mass. Council of Constr. Employers, Inc.*, 460 U.S. 204, 208 (1983). None of these cases is analogous to the facts here. In joining the Multistate Settlement Agreement, the States did not enter the tobacco market as a buyer or seller, nor did they assume control or ownership of any entity within the market. If we had found *Parker* immunity, the States' actions would not fall under the market participant exception to *Parker* immunity.

test. Although the States satisfy *Midcal*'s "clear articulation" prong, they fail the second prong requiring them to actively supervise the anticompetitive restraints causing injury. Because private participants in state action enjoy *Parker* immunity only to the extent the States enjoy immunity, the defendants are not shielded by *Parker*.[56] Therefore, consistent with the Supreme Court's treatment of hybrid restraints, we hold defendants are not immune under the *Parker* immunity doctrine.

IV.

Constitutional Claims

In its brief, and again at oral argument, plaintiffs asked us to find the Multistate Settlement Agreement unconstitutional under the Commerce Clause or the Compact Clause of the United States Constitution. But plaintiffs did not allege constitutional violations in their amended complaint, nor did the District Court address them. Therefore, these claims will not be addressed on appeal. *Mahone v. Addicks Utility Dist.*, 836 F.2d 921, 935 (5th Cir. 1988) ("It is black-letter law that '[a] motion to dismiss for failure to state a claim under Federal Rule of Civil Procedure 12(b)(6) is to be evaluated only on the pleadings.' ") (quoting *O'Quinn v. Manuel*, 773 F.2d 605, 608 (5th Cir. 1985)); *N.A.M.I. v. Essex County Bd. of Freeholders*, 91 F.Supp.2d 781, 787 n.7 (D.N.J. 2000) ("This Court need not consider claims that have not been pleaded in the complaint."); 5A Charles Alan Wright & Arthur R. Miller, *Federal Practice and Procedure*

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56. *See supra* note 35.

§ 1356 (1990). " 'Absent exceptional circumstances, an issue not raised in the district court will not be heard on appeal.' " *Walton v. Mental Health Ass'n of Southeastern Pa.*, 168 F.3d 661, 671 (3d Cir. 1999) (quoting *Altman v. Altman*, 653 F.2d 755, 758 (3d Cir. 1981)). When exceptional circumstances exist or to avoid "manifest injustice," issues not previously raised may be heard to protect the public interest. *See id.* No such interests are present. Although the Cato Institute, amicus curiae for plaintiffs, argues the constitutional claims, "new issues raised by an amicus are not properly before the court" in the absence of exceptional circumstances. *General Eng'g Corp. v. Virgin Islands Water and Power Auth. Caribbean Energy Co., Inc.*, 805 F.2d 88, 92 (3d Cir. 1986) (citing *United Parcel Serv. v. Mitchell*, 451 U.S. 56, 60 n.2 (1981)). These constitutional claims are not properly before us.[57]

V.

Conclusion

The Multistate Settlement Agreement creates novel issues because of the uniqueness of the instrument — involving forty-six states and over 98% of an industry. Although plaintiffs have properly pleaded an antitrust injury, the right to petition the government is paramount. Therefore, we hold defendants immune from antitrust liability under the *Noerr-Pennington* doctrine. But we find no immunity under the *Parker* doctrine. We will not address the constitutional issues.

We will affirm the judgment of the District Court.

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57. We note that plaintiffs failed to respond to defendants' briefing on this point.

Appendix A

TO THE CLERK:

Please file the foregoing opinion.

s/ Anthray J. Scirice
Circuit Judge

Appendix A

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 00-3410

A.D. BEDELL WHOLESALE COMPANY, INC.;
TRIANGLE CANDY & TOBACCO CO., on behalf of
themselves and all others similarly situated,

Appellants

v.

PHILIP MORRIS INCORPORATED;
R.J. REYNOLDS TOBACCO COMPANY, INC.;
BROWN AND WILLIAMSON TOBACCO CORP.

On Appeal from the United States District Court
for the Western District of Pennsylvania
D.C. Civil Action No. 99-cv-00558
(Honorable Donetta W. Ambrose)

Argued December 14, 2000

Before: SCIRICA, FUENTES and GARTH,
Circuit Judges

JUDGMENT

This cause came to be heard on the record from the United States District Court for the Western District of Pennsylvania and was argued by counsel on December 14, 2000.

Appendix A

On consideration whereof, it is now hereby ORDERED AND ADJUDGED by this Court that the Orders of the District Court entered March 22, 2000, and April 12, 2000, be, and the same are hereby affirmed. Costs taxed against appellants. All of the above in accordance with the opinion of this Court.

ATTEST:

s/ Marcia M. Waldron
Clerk

DATED: JUN 19 2001

APPENDIX B — OPINION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF PENNSYLVANIA DATED MARCH 22, 2000

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT
OF PENNSYLVANIA

Civil Action No. 99-558

A.D. BEDELL WHOLESALE COMPANY, INC., on behalf of itself and all others similarly situated,

Plaintiffs,

– vs –

PHILIP MORRIS, INCORPORATED, et al.,

Defendants.

AMBROSE, District Judge.

OPINION and ORDER OF COURT

Pending before the Court is the Joint Motion of Defendants Philip Morris Incorporated ("Philip Morris"), R.J. Reynolds Tobacco Company ("R.J. Reynolds") and Brown & Williamson Tobacco Corp. ("B&W") (collectively "the Defendants") to Dismiss the Complaint filed against them by Plaintiff A.D. Bedell Wholesale Company, Inc. ("Plaintiff") pursuant to Fed.R.Civ.P. 12(b)(6). Plaintiff has brought a putative class action against Defendants under

§ 1 and 2 of the Sherman Act, 15 U.S.C. §§ 1 and 2, and § 7 of the Clayton Act, 15 U.S.C. § 18. The primary basis for the motion to dismiss is that "[a]s a matter of law, plaintiff's Complaint fails to state a claim for relief under the anti-trust laws" in that "plaintiff's claims are barred in their entirety by either (or both) of two closely-related antitrust immunity doctrines: the Noerr-Pennington doctrine and the 'state action' doctrine." Defendants' Joint Memorandum of Law in Support of Their Motion to Dismiss the Complaint ("Defendants' Supporting Brief"), p. 3. Additionally, Defendants argue that Plaintiff's Third Claim for Relief ("Count III"), which is brought only against Defendant Philip Morris, must be dismissed for failure to state a claim under § 7 of the Clayton Act upon which relief can be granted. An amici curiae Brief in Support of the Defendants' Motion to Dismiss has been filed by certain state Attorneys General, all members of the Tobacco Committee of the National Association of Attorneys General "to the extent that Plaintiff seeks to impose antitrust liability upon the Defendants for the entering into settlement agreements with the sovereign states, and acts taken in compliance with the terms of such settlement agreements. Brief of Amici Curiae State Attorneys General ("Amici Curiae Brief"), p. 5.

STANDARD OF REVIEW

In deciding a motion to dismiss, all factual allegations and all reasonable inferences therefrom must be accepted as true and viewed in the light most favorable to the plaintiff. *Colburn v. Upper Darby Tp.*, 838 F.2d 663, 666 (3d Cir. 1988), *cert. den'd*, 489 U.S. 1065 (1989). A court may dismiss a plaintiff's complaint only if it appears beyond doubt

that the plaintiff can prove no set of facts in support of his claims which would entitle him to relief. *Conley v. Gibson*, 355 U.S. 41, 45 (1957). In ruling on a motion to dismiss for failure to state a claim, the court looks to "whether sufficient facts are pleaded to determine that the complaint is not frivolous, and to provide defendants with adequate notice to frame an answer." *Colburn*, 838 F.2d at 666.

FACTUAL BACKGROUND

In November, 1998, the Defendants entered into a settlement agreement (the "Master Settlement Agreement" or "MSA") with forty-six (46) states and six (6) other United States jurisdictions (collectively "the settling states") to settle lawsuits brought or threatened by the settling states for violation of their laws, including consumer protection and/or antitrust laws. MSA, Section 1. Various officials of the settling states (the attorney generals, governors, corporation counsel and mayors) signed the Master Settlement Agreement "on behalf of their respective Settling States." *Id.* The Master Settlement Agreement was voluntarily entered into by each of the settling states and the Defendants and is the result of arms-length negotiations between the parties to the Agreement. The stated reason for the settling states entering into the MSA was because "the undersigned Settling State officials believe that entry of this Agreement . . . with the tobacco industry is necessary in order to promote the Settling States' policies designed to reduce Youth smoking, to promote the public health and to secure monetary payments to the Settling States." MSA, Section 1.

Relevant for purposes of this action, the Master Settlement Agreement contains a clause, termed by Plaintiff

in its Complaint as the Renegade Clause. The Renegade Clause states: "[a] Subsequent Participating Manufacturer ("SPM") shall have payment obligations under this Agreement only in the event that its Market Share in any calendar year exceeds the greater of (1) its 1998 market share or (2) 125% of its 1997 market share." The Master Settlement Agreement also provides for the creation of a $50 million fund by the Attorneys General of the United States, acting through the National Association of Attorneys General ("NAAG"), which is to be maintained by the Attorneys General to supplement the settling states' enforcement and implementation of the terms of the Master Settlement Agreement and consent decrees and investigation and litigation of potential violation of laws with respect to tobacco products.

SUMMARY OF PLAINTIFF'S CLAIMS AGAINST THE DEFENDANTS

Count I of Plaintiff's Complaint alleges a violation of § 1 of the Sherman Act. More specifically, Count I of the Plaintiff's Complaint alleges that the Renegade Clause of the Master Settlement Agreement and the $50 million enforcement fund were made part of the Master Settlement Agreement by the Defendants as part of a conspiracy to prevent competition at a discount level by existing SPMs and nonparticipating manufacturers ("NPMs") and potential new entrants to the cigarette sales market and to raise and maintain the price of cigarettes in the U.S. cigarette market at artificially high levels. Thus, Plaintiff argues, the Master Settlement Agreement on its face sets forth a classic horizontal conspiracy to restrict output, allocate market

shares and raise prices between three competitors having nearly 90% of the market. In Count I, Plaintiff also alleges that the acts committed by the Defendants in furtherance of their unlawful conspiracy included the payment by Philip Morris to Liggett, a tobacco manufacturer and then a NPM in the MSA, of $300 million for the sale of three relatively insignificant brands of cigarettes which was conditioned upon Liggett signing the Master Settlement Agreement and the pressuring by the Defendants, through their own attorneys and indirectly through the NAAG and its private attorneys, of the few remaining small competitors to join the Master Settlement Agreement.

Count II of Plaintiff's Complaint alleges a violation of § 2 of the Sherman Act. More particularly, in Count II of the Complaint, Plaintiff alleges that the above-described alleged acts and agreements by the Defendants constitute a conspiracy in furtherance of Philip Morris' monopolization of the U.S. cigarette market in violation of § 2 of the Sherman Act in that the agreements and the acts taken in furtherance of the agreements were specifically intended to exclude and have in fact excluded meaningful price competition in the United States domestic cigarette market. Plaintiff further alleges in Count II that the acts of Philip Morris constitute monopolization and attempted monopolization of the U.S. cigarette market; that Philip Morris has and has had the specific intent to monopolize the U.S. cigarette market; and that there is a reasonable probability that it has or soon will have attained monopoly power in the U.S. cigarette market.

Count III of Plaintiff's Complaint alleges a violation of § 7 of the Clayton Act against Defendant Philip Morris only.

More specifically, Plaintiff alleges that Philip Morris paid Liggett to join the Master Settlement Agreement to remove Liggett as a competitive threat. Specifically, Plaintiff alleges that on November 20, 1998, three (3) days after the Master Settlement Agreement was signed, Philip Morris purchased three brands of premium cigarettes from Liggett which constituted about two-thirds of the 2% of the overall domestic cigarette market that were sold by NPMs (or 0.2% of the domestic cigarette market) in exchange for Liggett's agreement to become a SPM in the MSA. Plaintiff further alleges that this acquisition would constitute a purchase of assets illegal under § 7 of the Clayton Act in that its effect may be, and has been, to substantially lessen competition and to further or create a monopoly in the sale of domestic cigarettes. Plaintiff argues that until that time Liggett was a NPM and although NPMs comprised only approximately 2% of the overall domestic cigarette market, they represented a clear and present danger of price competition. Liggett sales made up about two-thirds of that 2% and therefore, Plaintiff argues, having Liggett join the Master Settlement Agreement was a necessary step to eliminating virtually all price competition with the domestic tobacco market.

LEGAL ANALYSIS

A. *Counts I and II: Sherman Act claims.*

1. Application of Noerr-Pennington immunity doctrine.

Defendants first argue that the claims asserted against them in Plaintiff's Complaint must be dismissed in their entirety in light of the Noerr-Pennington immunity doctrine

because "the *Noerr-Pennington* doctrine also confers antitrust immunity upon litigation activities of competitors," "[l]itigation settlements with the government are indisputably within the scope of *Noerr-Pennington* immunity," "it is well-established that the *Noerr-Pennington* . . . doctrine [is] applicable even if the alleged conduct would otherwise be deemed 'illegal per se' under the antitrust laws," and "the M.S.A. was an agreement *with the government* (rather than a mere agreement with other *private* parties), [and therefore,] it would also be entitled to Noerr-Pennington protection as a government contract, even if it had not been executed to resolve pending and threatened litigation." Defendants' Supporting Brief, pp. 5-6, 8-10.

As explained by the United States Court of Appeals for the Third Circuit in *Cheminor Drugs, Ltd. v. Ethyl Corp.*, 168 F.3d 119, 122 (3d Cir.), *cert. den' d*, 120 S.Ct. 173 (1999):

> [a] party who petitions the government for redress generally is immune from antitrust liability. This immunity extends to persons who petition all types of government entities — legislatures, administrative agencies, and courts. "[W]here restraint upon trade or monopolization is the result of valid governmental action, as opposed to private action, no violation of the [Sherman] Act can be made out."
>
> Noerr-Pennington does not apply, however to petitions or lawsuits that are a "mere sham to cover what is actually nothing more than an

> attempt to interfere directly with the business relationships of a competitor." Often, a petition to the government causes an anticompetitive effect, but "evidence of anticompetitive intent or purpose alone cannot transfer otherwise legitimate activity into a sham."

Id. at 122 (internal citations omitted). *See also City of Columbia v. Omni Outdoor Advertising, Inc.*, 499 U.S. 365 (1991) ("[t]he 'sham' exception to *Noerr* encompasses situations in which persons use the governmental *process* — as opposed to the *outcome* of that process — as an anticompetitive weapon . . . . A 'sham' situation involves a defendant whose activities are 'not genuinely aimed at procuring favorable governmental action' at all [citation omitted] not one 'who genuinely seeks to achieve his governmental result, but does so *through improper* means'."); *We, Inc. v. City of Philadelphia*, 174 F.3d 322, 326 (3d Cir. 1999) ("[t]he Noerr-Pennington doctrine originated in the anti-trust context as the proposition that 'joint efforts to influence public officials do not violate the antitrust laws even though intended to eliminate competition. Such conduct is not illegal, either standing alone or as part of a broader scheme itself violative of the Sherman Act'.").

Relevant to the case *sub judice* is the decision of the United States District Court for the Northern District of Oklahoma in *Hise v. Philip Morris Inc.*, 46 F.Supp.2d 1201 (N.D. Ok. 1999), *aff'd*, 2000 WL 192892 (10th Cir. Feb. 18, 2000). *Hise* involved the very same defendants as in the case at bar and involved claims by the plaintiffs, consumers of the defendants' tobacco products, that the defendants had

violated federal antitrust laws by negotiating and entering into the MSA. Defendants argue that said activity was protected under the Noerr-Pennington doctrine as conduct incidental to litigation and as a contract entered into with the government:

> Defendants assert that subsequent to being sued by over 40 states in the respective state courts, they entered into the M.S.A. to compromise these lawsuits. Defendants contend that the M.S.A. represents defendants' petitioning of the settling states and the judiciary. Defendants further argue that the M.S.A. is protected as a contract with government officials. Defendants point to plaintiffs' concession that the M.S.A. was a compromise agreement reached between defendants and the several states that had initiated lawsuits against defendants. Defendants therefore maintain that both the negotiation phase and the resulting agreement with the states fall within the protections afforded by the Noerr-Pennington doctrine.

Id. at 1205-06. Ultimately, the *Hise* district court concluded that the defendants' activities "in negotiating the M.S.A. with the settling states and achieving a settlement agreement with those states are protected under the Noerr-Pennington doctrine as conduct incidental to litigation." *Id.* at 1206. *See also id.* at 1207 ("[t]he Court finds that the actions of defendants in negotiating and executing the M.S.A. fall within the recognition that 'Noerr shields from the Sherman Act a concerted effort to influence public officials regardless

of intent or purpose' . . . and therefore concludes that the concerted effort by defendants to influence public officials, i.e., the states' Attorney General, to accept a settlement in exchange for dismissing the numerous lawsuits pending against defendants is among the activities protected by the Noerr-Pennington doctrine."). In so holding, the court reasoned "[t]he Court agrees with defendants that the doctrine would surely ring hollow if it failed to encompass private entities who, after having been sued by one or more states for similar conduct, jointly petition the states in order to achieve a mutually acceptable settlement, designed to reduce the amount of time and expense involved in defending the action." *Id.* Moreover, the *Hise* court explained that under the Noerr-Pennington doctrine, "the fact that the private defendants' motives are selfish is irrelevant" as is "the fact that the result may have anti-competitive consequences." *Id.*, *citing*, *City of Columbia v. Omni Outdoor Advertising, Inc.*, 499 U.S. 365, 380 (1991); *Greenwood Utilities Com'n v. Mississippi Power Co.*, 751 F.2d 1484, 1497 (5th Cir. 1985). Significantly, the district court's decision in *Hise* was recently affirmed by the United States Court of Appeals in *Hise and Isch v. Philip Morris Inc. et al.*, 2000 WL 192892 (10th Cir. Feb. 18, 2000). In the appellate decision, the court first explained: "the district court rejected [the plaintiffs'] first claim that the settlement agreement violates the Sherman Anti-Trust Act" and "[i]n so holding, the district court determined the tobacco companies' action in negotiating and executing the settlement agreement fell under the protections of the 'Noerr-Pennington' doctrine which shields from the Sherman Anti-Trust Act any concerted effort to influence public officials, regardless or intent or purpose." *Id.* The appellate court then stated that "we must agree with

the district court that summary judgment should be granted in favor of the tobacco companies," that "[b]ecause the district court issued a well-reasoned decision, thoroughly explaining the reasons for granting summary judgment . . . we decline to duplicate its analysis here," and ultimately concluded "[f]or the reasons contained herein, and for substantially the same reasons articulated in the district court's April 29, 1999 decision, we AFFIRM summary judgment in favor of the Appellee tobacco companies".[1] *Id.*

After careful consideration of the submissions of the parties, as did the *Hise* courts, I conclude that to the extent Plaintiff's antitrust claims are based upon the Defendants' actions in negotiating and executing the MSA, said actions fall within the category of conduct protected by the Noerr-Pennington immunity doctrine and are not subject to the "sham" exception to the Noerr-Pennington immunity doctrine. Accordingly, to the extent Plaintiff's antitrust claims found in Counts I and II of the Complaint are based upon the Defendants' actions in negotiating and executing

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1. Notably, the appellate court also explained that the plaintiff in the case *sub judice*, A.D. Bedell Wholesale Company Inc., had filed an amicus curiae brief with the appellate court claiming that the district court had "sweepingly applied the 'Noerr-Pennington doctrine' without the necessary 'closer examination of the terms of the [settlement agreement] itself and the circumstances pursuant' thereto" and that both the tobacco defendants and A.D. Bedell had subsequently filed motions with accompanying briefs with respect to the amicus brief, that the court was denying both motions because supplemental responses were not necessary, but that "in doing so, we note we have reviewed the responsive briefs, and conclude that even if considered, they would not affect our disposition in this case." *Id.* at n.3.

the MSA, these claims are dismissed for failure to state a Sherman Act claim upon which relief can be granted.

2. Application of Parker State Action immunity doctrine.

Defendants contend that all of the antitrust claims against them must be dismissed because they are immune with respect to these actions under the state action immunity doctrine. In articulating the state action immunity doctrine, the United States Court of Appeals for the Third Circuit explained: "[i]n *Parker v. Brown* the Supreme Court held that the Sherman Act does not prohibit an anticompetitive restraint imposed by a state as an act of government." *Massachusetts School of Law at Andover, Inc. v. American Bar Assoc.*, 107 F.3d 1026, 1035 (3d Cir. 1997), *cert. den'd*, 522 U.S. 907 (1997).

To the extent the Plaintiff's Complaint is premised upon it being injured by the Defendants' conduct of entering into, executing and implementing the Master Settlement Agreement and in engaging in conduct mandated under the terms of the Master Settlement, I conclude that the first step in determining whether the state action immunity doctrine is applicable to said conduct must be to determine whether the same conduct by the settling states, i.e. in entering into, executing, and implementing the MSA, would be subject to state action immunity. Under the facts of this case, this conduct was action taken both by the Defendants and by the settling states and was mandated by the terms of the MSA.

After careful consideration of the submissions of the parties and the *amici curiae*, I conclude that because

the conduct of entering into, executing and implementing the MSA was undertaken by the settling states functioning in their sovereign capacities, to the extent Plaintiff's injuries are premised upon said conduct, liability for said conduct by the states would be subject to *Parker* state action immunity. Obviously in so holding, I opine, contrary to the argument presented by Plaintiff, that in this case, application of the *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 100 S.Ct. 937 (1980) test is inappropriate. *See Massachusetts School of Law at Andover, Inc.*, 107 F.3d at 1035 ("[b]ecause the states are sovereign in imposing the bar admission requirements, the clear articulation and active supervision requirements urged by [plaintiff] are inapplicable.").

Having so determined, I further conclude that to the extent Plaintiff alleges that its injuries were caused by the Defendants entering into, implementing and executing the Master Settlement Agreement with the settling states and in engaging in conduct mandated under the terms of the Master Settlement Agreement, said conduct similarly is protected under the state action immunity doctrine. To allow otherwise "would allow the Parker doctrine to be circumvented by artful pleading: 'A plaintiff could frustrate any [Parker protected state plan] merely by filing suit against the regulated private parties, rather than the state officials who implement the plan'." *Charley's Taxi Radio Dispatch Corp. v. SIDA of Hawaii, Inc.*, 810 F.2d 869, 878 (9th Cir. 1987), *quoting, Southern Motor Carriers Rate Conference, Inc. v. U.S.*, 471 U.S. 48, 105 S.Ct. 1721, 1727 (1985). *See also Automated Salvage Transport, Inc. v. Wheelabrator Environmental Systems, Inc.*, 155 F.2d 59, 74 (2d Cir. 1998) (holding that

once it was determined that state immunity protected state solid waste authority from liability under Sherman Act with respect to settlement agreement it entered into with private party defendants, private defendants were also protected under state action doctrine: "our conclusion that [the state entity] can avail itself of the Parker doctrine also compels the conclusion that the [private party] defendants are shielded from antitrust liability. Subjecting them to antitrust liability would effectively block [the state entity's] efforts to carry out its mandate through contracts with private parties"); *Armstrong Surgical Center, Inc. v. Armstrong County Memorial Hospital*, 185 F.3d 154, 159 (3d Cir. 1999) (noting, in discussing the *Noerr-Pennington* doctrine, "if relief is sought solely for injury as to which the state would enjoy immunity under *Parker*, the private petitioner also enjoys immunity."). Thus, to the extent Plaintiff's Sherman Act anti-trust claims against Defendants, found in Counts I and II of the Complaint, are premised upon the Defendants entering into, implementing and executing the Master Settlement Agreement with the settling states and engaging in conduct mandated under the terms of the Master Settlement Agreement, these claims must be dismissed for failure to state a claim upon which relief can be granted.

3. Plaintiff's Sherman Act claims with respect to Philip Morris' conduct towards Liggett and Defendants' conduct towards other manufacturers of domestic cigarettes.

It must be emphasized that the analyses and holdings of this Court thus far have been limited to the injuries allegedly sustained by Plaintiff as a result of the Defendants' conduct

in negotiating, entering into, implementing and executing the Master Settlement Agreement with the settling states and in engaging in conduct mandated under the terms of the Master Settlement Agreement. My analyses and holdings have not addressed the Plaintiff's allegations of violation of the Sherman Act with respect to Philip Morris buying three brands of cigarettes from Liggett in order to coerce its signing the Master Settlement Agreement or the conduct of the Defendants in coercing smaller manufacturers of domestic cigarettes to sign the MSA.

Defendants do, however, attack the viability of these allegations while discussing the applicability of the state action immunity doctrine to the allegations of the case at bar. *See* Defendants' Supporting Brief, p. 16.

After careful consideration of the submissions of the parties on this issue, I find that the state action immunity doctrine is applicable to the Plaintiff's claims that Defendants violated the Sherman Act in this regard. Specifically, I find that because the injury allegedly suffered by Plaintiffs as a result of the Defendants' alleged acts of coercion is an incidental effect of the conduct of the Defendants and the settling states in entering into, executing and implementing the MSA, conduct which I have held to be immune under the state action immunity doctrine, the state action immunity doctrine also applies to bar Plaintiff's anti-trust claims based upon said coercive acts. *See Massachusetts School of Law at Andover, Inc.*, 107 F.3d at 1035.

Appendix B

4. Summary.

For the above-stated reasons, Counts I and II of Plaintiff's Complaint are dismissed in their entirety.

B. *Count III — Plaintiff's § 7 Clayton Act claim against Defendant Philip Morris.*

In Count III of the Complaint, brought only against Defendant Philip Morris, Plaintiff alleges a violation of § 7 of the Clayton Act. The allegations underlying this claim have been set forth *supra.*, and need not be repeated. Defendant Philip Morris moves to dismiss this claim against it on several bases. First, Philip Morris argues that this claim is only another antitrust challenge to the legality of the MSA, that Plaintiff alleges that because the MSA is unlawful, it was also unlawful for Phillip Morris to acquire the Liggett brands in order to induce Liggett to join the MSA which is necessarily premised upon the alleged illegality of the MSA. Therefore, Philip Morris contends that the claim should be dismissed on the same immunity grounds as the rest of the Complaint. Second, Philip Morris contends that Plaintiff's alleged injury from the acquisition by Philip Morris of the Liggett brands does not constitute an anti-trust injury because "[a] plaintiff suffers 'antitrust injury' from an acquisition only if its injury is caused by the increase in market power that the acquired assets confer upon the acquiring firm." Defendants' Supporting Brief, p. 23. In the case at bar, Philip Morris argues that "[b]ecause plaintiff concedes that the brands acquired by Philip Morris are 'insignificant,' the acquisition of these brands, as a matter of law, could not increase Philip Morris' market power and thus could not

cause 'antitrust injury' to plaintiff." *Id.* Third, Philip Morris argues that while Plaintiff alleges that it was injured by Liggett's decision to join the MSA, under *Alberta Gas Chemicals Ltd. v. E.I. Du Pont De Nemours and Co.*, 826 F.2d 1235, 1241 (3d Cir. 1987), *cert. den'd*, 486 U.S. 1059 (1988), such an allegation does not constitute "antitrust injury" resulting from an asset acquisition. Fourth, Philip Morris argues that to the extent Plaintiff is alleging that this acquisition is unlawful without regard to the MSA, § 7 of the Clayton Act only prohibits acquisitions that are likely "substantially to lessen competition," "[a]n acquisition cannot cause substantial injury to competition if it does not result in a 'significant' increase in the acquiring firm's market share." *Id.* Here Plaintiff alleges that the three brands purchased by Philip Morris are "insignificant" and together account for only 0.2% of cigarette sales in the United States, a *de minimis* amount. "Because plaintiff's own allegations confirm that Philip Morris' acquisition of the three brands acquired from Liggett cannot have a *significant* competitive impact, the Complaint fails to state a claim for relief under Clayton Act § 7." *Id.* at 24. Finally, in Defendants' Joint Reply Brief in Further Support of Their Motion to Dismiss the Complaint ("Defendants' Reply Brief"), Philip Morris argues that an acquisition is unlawful only if it will substantially harm competition, that the only allegation in Plaintiff's Complaint as to how the acquisition of the Liggett brands impairs competition is the allegation that the acquisition induced Liggett to join the MSA, and that because this allegation obviously depends upon a finding that the MSA itself is unlawful, the Clayton Act claim must be dismissed if the MSA is entitled to antitrust immunity. Defendants' Reply Brief, p. 10.

In response, Plaintiff argues that Philip Morris misstates its Clayton Act claim when it contends that said claim is "simply another antitrust challenge to the legality of the MSA" or that its injury arises from Liggett's decision to join the MSA. Plaintiff's Opposition Brief, p. 21, *citing* Defendants' Supporting Brief, p. 22. "While Liggett's execution of the MSA contributed to further concentration in the market, it was Philip Morris' acquisition — not Liggett's decision to join the MSA — is what violates § 7; and plaintiff, as a direct purchaser in the market where such acquisition may substantially lessen competition or tend to create a monopoly in Philip Morris, unequivocally has standing to sue for injunctive relief." *Id.* Plaintiff also argues that "[a]n antitrust plaintiff seeking injunctive relief for violation of § 7 need only show a threatened injury, not an actual one." *Id.* Plaintiff further argues that its injury flows from the fact that it is a purchaser and reseller of cigarettes and Philip Morris now controls the supply of cigarettes. Therefore, Plaintiff argues, it is thus forced to operate in a market controlled by a monopolist rather than market forces. *Id.* Third, Plaintiff argues that Philip Morris' *de minimis* argument is not applicable here because in the case at bar there exists a highly concentrated market with significant barriers to entry and therefore, "even the slightest gain in market share via an acquisition violates § 7." *Id.* at 22.

After careful consideration of the submissions of the parties, I find as follows. First, given that Plaintiff's Clayton Act claim against Philip Morris is not premised upon Liggett's involvement in the Master Settlement Agreement, but rather, is based upon Philip Morris' acquisition of the Liggett brands allegedly to substantially lessen competition

and to further or create a monopoly in the sale of domestic cigarettes, neither the Noerr-Pennington nor the Parker state action immunity doctrines are applicable. Further, I find that because Plaintiff's Clayton Act claim against Philip Morris is based upon Philip Morris' acquisition of the Liggett brands allegedly to substantially lessen competition and to further or create a monopoly in the sale of domestic cigarettes, it is not necessary to substantively address those arguments raised by Philip Morris that are premised upon Plaintiff's Clayton Act claim being based upon Liggett's involvement in the Master Settlement Agreement.

Finally, I find that because a claim for relief should only be dismissed at the motion to dismiss stage if it appears beyond doubt that the plaintiff can prove no set of facts in support of its claims which would entitle it to relief, it would be improper to dismiss Count III of Plaintiff's Complaint for failure to state a claim upon which relief can be granted. This is so because Plaintiff has alleged that Philip Morris' acquisition may be and has been to substantially lessen competition in the domestic cigarette market, and to further or create a monopoly in the sale of domestic cigarettes. Complaint, ¶ 104. Additionally, Plaintiff has alleged that Defendants collectively account for 89% of all cigarettes sold in the domestic cigarette market, Philip Morris has a 52% total market share in the market and sells more than 60% of premium brand cigarettes, and barriers to entry in the U.S. market for cigarettes are substantial. *Id.* at ¶¶ 3 and 24. *See U.S. v. Aluminum Co. of America*, 377 U.S. 271, 278 (1964) (holding that acquisition by Alcoa of stock and assets of another company violated § 7 of the Clayton Act where Alcoa had controlled from 27.8% to 32.5% of the aluminum

conductor market, acquisition added 1.3% to Alcoa's control of the market and market was highly concentrated); *F.T.C. v. PepsiCo, Inc.*, 477 F.2d 24, 27 (2d Cir. 1973) (holding in context of action for preliminary injunction that acquisition by PepsiCo of stock of another company likely violated § 7 of Clayton Act and Section 5 of the Federal Trade Commission Act where, *inter alia*, PepsiCo occupied 16.3% of soft drink concentrates market, PepsiCo and Coca Cola combined to control 58.3% of market, the top four companies accounted for 70.6% of market and soft drink business was not easily entered and acquisition would give PepsiCo another 1% of the soft drink non-cola market and .3% of the soft drink market); *Stanley Works v. F.T.C.*, 469 F.2d 498, 507-08 (2d Cir. 1972), *cert. den'd*, 412 U.S. 928 (1973) (holding that company with 1% of market's acquisition of another company with 22%-24% market share was a violation of § 7 of the Clayton Act and not *de minimis* where four companies dominated 50% of the market). Accordingly, Defendants' Motion to Dismiss Plaintiff's claim against Philip Morris for violation of § 7 of the Clayton Act is denied.

DATE FILED: MARCH 22, 2000

* * *

Appendix B

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT
OF PENNSYLVANIA

Civil Action No. 99-558

A.D. BEDELL WHOLESALE COMPANY, INC., on behalf of itself and all others similarly situated,

Plaintiffs,

– vs –

PHILIP MORRIS, INCORPORATED, et al.,

Defendants.

AMBROSE, District Judge.

ORDER OF COURT

AND NOW, this **22nd** day of March, 2000, after careful consideration of the submissions of the parties and for the reasons stated in the Opinion accompanying this Order, it is **ORDERED** that the Defendants' Motion to Dismiss (Docket No. 15) is **GRANTED** as to Counts I and II of the Plaintiff's Complaint and is **DENIED** as to Count III of the Plaintiff's Complaint.

Defendants are **ORDERED** to file an Answer to Count III by **April 24, 2000**. A Status Conference is scheduled for

Appendix B

Tuesday, April 25, 2000 at 9:00 A.M. before the undersigned in Room 620 of the United States Post Office and Courthouse. Counsel shall have settlement authority.

BY THE COURT:

s/ Donetta W. Ambrose
Donetta W. Ambrose,
U.S. District Judge

APPENDIX C — CONSENTED-TO ORDER OF THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF PENNSYLVANIA DATED APRIL 11, 2000

IN THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF PENNSYLVANIA

Civil Action No. 99-558

JURY TRIAL DEMANDED

A.D. BEDELL WHOLESALE COMPANY, INC. and TRIANGLE CANDY & TOBACCO CO., on behalf of themselves and all others similarly situated,

Plaintiffs,

v.

PHILIP MORRIS INCORPORATED, R.J. REYNOLDS TOBACCO COMPANY, INC. and BROWN & WILLIAMSON TOBACCO CORP.,

Defendants.

CONSENTED-TO ORDER

AND NOW, this 11th day of April, 2000, and with the consent of the plaintiffs and Philip Morris Incorporated, which is the only defendant to the claims asserted in Count III of the Amended Complaint-Class Action in this matter,

Appendix C

IT IS HEREBY ORDERED that Count III of the Amended Complaint-Class Action is DISMISSED WITHOUT PREJUDICE.

As this dismissal without prejudice disposes of all remaining claims in this action, IT IS FURTHER ORDERED that the Clerk is to enter judgment in this action in favor of the defendants, Philip Morris Incorporated, R.J. Reynolds Tobacco Company, Inc. and Brown & Williamson Tobacco Corp., and against the plaintiffs, A.D. Bedell Wholesale Company, Inc. and Triangle Candy & Tobacco Co.

s/ Donetta W. Ambrose, J.

CONSENTED TO:

s/ William M. Wycoff
William M. Wycoff
Counsel for Plaintiffs

s/ Bernard D. Marcus
Bernard D. Marcus
Counsel for Philip Morris Incorporated

APPENDIX D — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT DENYING PETITION FOR REHEARING DATED JULY 24, 2001

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 00-3410

A.D. BEDELL WHOLESALE COMPANY, INC.;
TRIANGLE CANDY & TOBACCO CO., on behalf of themselves and all others similarly situated,

Appellants

v.

PHILIP MORRIS INCORPORATED;
R.J. REYNOLDS TOBACCO COMPANY, INC.;
BROWN AND WILLIAMSON TOBACCO CORP.

(D.C. Civ. No. 99-cv-00558)

SUR PETITION FOR REHEARING

Present: SLOVITER, MANSMANN, SCIRICA, NYGAARD, ALITO, ROTH, McKEE, BARRY, AMBRO, FUENTES and GARTH*, *Circuit Judges*

The petition for rehearing filed by appellants in the above-entitled case having been submitted to the judges who

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* As to panel rehearing only.

participated in the decision of this Court and to all the other available circuit judges of the circuit in regular active service, and no judge who concurred in the decision having asked for rehearing, and a majority of the circuit judges of the circuit in regular service not having voted for rehearing, the petition for rehearing by the panel and the Court en banc, is denied.

BY THE COURT,

s/ [illegible]
Circuit Judge

Dated: JUL 24 2001

Supreme Court, U.S.
FILED
NOV 21 2001

No. 01-656

IN THE

Supreme Court of the United States

A.D. BEDELL WHOLESALE COMPANY, INC., TRIANGLE CANDY & TOBACCO CO., on behalf of themselves and all others similarly situated,
Petitioners,

v.

PHILIP MORRIS INCORPORATED, R.J. REYNOLDS TOBACCO COMPANY, INC., BROWN AND WILLIAMSON TOBACCO CORP.,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Third Circuit

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1) Whether the Court of Appeals correctly applied the *Noerr-Pennington* doctrine in holding that Respondents were not liable under the antitrust laws for successfully petitioning state governments to resolve the litigation that these state governments had filed against them.

2) Whether the Court of Appeals correctly declined to address constitutional claims that Petitioners had not alleged in their complaint.

3) Whether the judgment of the Court of Appeals could also be sustained on an alternative ground relied upon by the District Court – namely, that Respondents' settlement with state governments constitutes "state action" under the *Parker v. Brown* doctrine.

LIST OF PARTIES AND CORPORATE DISCLOSURE STATEMENT

All parties to the proceeding in the Third Circuit are listed in the caption on the cover of this Brief in Opposition. Pursuant to Supreme Court Rule 29.6, Respondents identify the following parent corporations and publicly held corporations owning ten percent or more of Respondents' stock:

Philip Morris Incorporated:
Philip Morris Companies Inc.

R. J. Reynolds Tobacco Company, Inc.:
R. J. Reynolds Tobacco Holdings, Inc.

Brown & Williamson Tobacco Corp.:
B.A.T. Industries p.l.c.
BATIC Inc.
BATUS Holdings Inc.
BATUS Tobacco Services, Inc.
British American Tobacco p.l.c.
British American Tobacco (1998) Ltd.
British-American Tobacco (Holdings) Ltd.
Louisville Securities Ltd.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
LIST OF PARTIES AND CORPORATE DISCLOSURE STATEMENT	ii
TABLE OF CITED AUTHORITIES	v
PRELIMINARY STATEMENT	1
STATEMENT OF THE CASE	3
REASONS FOR DENYING THE WRIT	6
I. THERE IS NO CONFLICT: THE DECISION BELOW APPLIES *NOERR-PENNINGTON* TO THE MSA IN PRECISELY THE SAME MANNER AS EVERY OTHER COURT THAT HAS ADJUDICATED CHALLENGES TO THE MSA	7
II. THE DECISION BELOW MAKES NO NEW LAW: THE COURT OF APPEALS' APPLICATION OF *NOERR-PENNINGTON* RELIES UPON AND ADHERES TO APPLICABLE PRECEDENTS FROM THIS COURT AND OTHER COURTS OF APPEALS	10
III. PETITIONERS DID NOT ALLEGE THAT THE MSA VIOLATES THE COMMERCE CLAUSE AND THE INTERSTATE COMPACT CLAUSE, AND IN ANY EVENT, THEIR CONSTITUTIONAL ARGUMENTS ARE IRRELEVANT	18

TABLE OF CONTENTS – Continued

Page

IV. THIS COURT SHOULD NOT GRANT THE WRIT BECAUSE THE JUDGMENT BELOW CAN ALSO BE DEFENDED ON AN ALTERNATIVE GROUND 21

CONCLUSION 25

TABLE OF CITED AUTHORITIES

FEDERAL CASES Page

Allied Tube & Conduit Corp. v. Indian Head, Inc., 486 U.S. 492 (1988).....14, 15, 16
Andrx Pharms., Inc. v. Biovail Corp., 256 F.3d 799 (D.C. Cir. 2001)..... 13, 14
Automated Salvage Transp., Inc. v. Wheelabrator Envtl. Sys., Inc., 155 F.3d 59 (2d Cir. 1998)..... 23, 24
Bates v. State Bar of Ariz., 433 U.S. 350 (1977)... 19
Bonollo Rubbish Removal, Inc. v. Town of Franklin, 886 F. Supp. 955 (D. Mass. 1995)..... 18
Bright v. Ogden City, 635 F. Supp. 31 (D. Utah 1986), *aff'd sub nom. Bright v. Moss Ambulance Serv., Inc.*, 824 F.2d 819 (10th Cir. 1987)..... 18
Broadcast Music, Inc. v. Columbia Broadcasting Sys., Inc., 441 U.S. 1 (1979)..... 12, 13
Cal. Motor Transp. Co. v. Trucking Unlimited, 404 U.S. 508 (1972).....8, 10, 11, 12
Cal. Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc., 445 U.S. 97 (1980)..... 17
Campbell v. City of Chicago, 823 F.2d 1182 (7th Cir. 1987)..... 12
City of Columbia v. Omni Outdoor Adver., Inc., 499 U.S. 365 (1991)..... *passim*
Coastal States Mktg. v. Hunt, 694 F.2d 1358 (5th Cir. 1983)..... 12
Columbia Pictures Indus., Inc. v. Prof'l Real Estate Investors, Inc., 944 F.2d 1525 (9th Cir. 1991), *aff'd on other grounds*, 508 U.S. 49 (1993)..... 12
Demarest v. Manspeaker, 498 U.S. 184 (1991)..... 19
E. R.R. Presidents Conference v. Noerr Motor Freight, Inc., 365 U.S. 127 (1961)..... *passim*

TABLE OF CITED AUTHORITIES – Continued

Page

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Forces Action Project LLC v. California, No. C 99-0607 MJJ, 2000 WL 20977 (N.D. Cal. Jan. 5, 2000) 9

FTC v. Superior Court Trial Lawyers Ass'n, 493 U.S. 411 (1990) 16

Granfinanciera, S.A. v. Nordberg, 492 U.S. 33 (1989) 22

Gray v. Netherland, 518 U.S. 152 (1996) 19

Greenwood Utils. Comm'n v. Miss. Power Co., 751 F.2d 1484 (5th Cir. 1985) 15, 19

Hise v. Philip Morris Inc., 531 U.S. 959 (2000) 2, 6

Hise v. Philip Morris Inc., No. 99-5113, 2000 WL 192892 (10th Cir. Feb. 17, 2000) 9

Hise v. Philip Morris Inc., 46 F. Supp. 2d 1201 (N.D. Okla. 1999) 8, 20

Hoover v. Ronwin, 466 U.S. 558 (1984) 22

In re Cardizem CD Antitrust Litig., 105 F. Supp. 2d 618 (E.D. Mich. 2000) 13, 14

N. Am. Trading Co. v. Nat'l Ass'n of Attorneys Gen., No. 01-CV-1600 (D.D.C. Sept. 18, 2001), *appeal docketed*, No. 01-7173 (D.C. Cir. Oct. 17, 2001) 20

Parker v. Brown, 317 U.S. 341 (1943) ..... *passim*

Premium Tobacco Stores, Inc. v. Fisher, 51 F. Supp. 2d 1099 (D. Colo. 1999) 20

PrimeTime 24 Joint Venture v. NBC, Inc., 219 F.3d 92 (2d Cir. 2000) 13

PTI, Inc. v. Philip Morris Inc., 100 F. Supp. 2d 1179 (C.D. Cal. 2000) ..... *passim*

TABLE OF CITED AUTHORITIES – Continued

Page

Sessions Tank Liners, Inc. v. Joor Mfg., Inc., 17 F.3d 295 (9th Cir. 1994) 15

S. Motor Carriers Rate Conference v. United States, 471 U.S. 48 (1985) 17

Star Scientific, Inc. v. Early, No. 3:00CV835 (E.D. Va. Mar. 26, 2001), *appeal docketed*, No. 01-1502 (4th Cir. Apr. 19, 2001) 20

Subscription Television, Inc. v. S. Cal. Theatre Owners Ass'n, 576 F.2d 230 (9th Cir. 1978) 19

United Mine Workers of Am. v. Pennington, 381 U.S. 657 (1965) ..... *passim*

Washington v. Yakima Indian Nation, 439 U.S. 463 (1979) 22

Yee v. Escondido, 503 U.S. 519 (1992) 19

FEDERAL STATUTES

42 U.S.C. § 1396b(d)(3)(B) (2001) 5, 20

Fed. R. Civ. P. 12(b)(6) 5

TREATISES

1 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* (2d ed. 2000) 14, 16, 18, 20

IN THE

Supreme Court of the United States

No. 01-656

A.D. BEDELL WHOLESALE COMPANY, INC.,
TRIANGLE CANDY & TOBACCO CO., on behalf of
themselves and all others similarly situated,
Petitioners,

v.

PHILIP MORRIS INCORPORATED,
R.J. REYNOLDS TOBACCO COMPANY, INC.,
BROWN AND WILLIAMSON TOBACCO CORP.,
Respondents.

**On Petition for Writ of Certiorari to the
United States Court of Appeals
for the Third Circuit**

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

PRELIMINARY STATEMENT

Petitioners are two cigarette wholesalers who contend that Respondent cigarette manufacturers violated the antitrust laws by successfully petitioning state governments to settle litigation against them. Petitioners attack this settlement even though it (i) was negotiated with the state attorneys general, (ii) was approved by state and federal courts in the states, and (iii) was subsequently endorsed by the legislatures of the states.

The Court of Appeals unanimously affirmed the District Court's ruling that Respondents' conduct was immune from antitrust liability under the well-established *Noerr-Pennington* doctrine. This decision makes no new law. This Court has expressly held that *Noerr-Pennington* applies to the petitioning of state governments and to litigation-related conduct. Several other courts have adjudicated challenges to this same settlement, and all of these courts applied the *Noerr-Pennington* doctrine in exactly the same fashion as the Court of Appeals below. Indeed, this Court has already denied certiorari in one of these cases. *Hise v. Philip Morris Inc.*, 531 U.S. 959 (2000).

Petitioners strain to concoct a conflict regarding the application of the *Noerr-Pennington* doctrine, but their effort is futile. No case supports Petitioners' contentions that *Noerr-Pennington* immunity does not apply to private litigants who petition the government to resolve litigation against them, or that *Noerr-Pennington* immunity protects only the petitioning process and not the government's response to such petitioning. To the contrary, this Court's decisions in the *Noerr* and *Pennington* cases recognized that antitrust immunity protects private parties *not only* from claims arising from their efforts to petition the government, *but also* from claims arising from any "restraints" that the government implements in response to such petitioning. *See infra* pp. 14-16. Petitioners' complaint challenged the litigation settlement *with the states*, along with the statutes enacted *by the states* to further the settlement's purposes. *Noerr-Pennington* unquestionably protects private parties from antitrust liability for such "post-petitioning" conduct involving the government, as this Court has consistently held.

In the absence of any real conflict, Petitioners argue that the Court of Appeals incorrectly "applied" the *Noerr-Pennington* doctrine to the facts of this case, and that this Court should grant certiorari in order to "brighten[] the

demarcation line" between the *Noerr-Pennington* doctrine and the *Parker* ("state action") doctrine. Pet. at 19-20. Yet there is no line that is in need of "brightening." Any confusion between these two doctrines rests solely with Petitioners. The Court of Appeals' application of *Noerr-Pennington* follows longstanding precedents of this Court, which clearly establish the parameters of the *Noerr-Pennington* doctrine.

STATEMENT OF THE CASE

1. *Factual Background.* In 1998, Respondents successfully petitioned forty-six states (as well as the District of Columbia and five territories) to enter into the Master Settlement Agreement ("MSA"), a comprehensive resolution of lawsuits brought by these states against Respondents, seeking monetary and injunctive relief (the "State Lawsuits").[1] The State Lawsuits "[e]ndeavor[ed] to recoup billions of dollars in public health care costs and to reduce cigarette smoking . . . ." App. 2a. Under the MSA, the states have required Respondents, *inter alia*, to restrict their cigarette marketing and advertising activities, to fund a program of public education to deter youth smoking, and to make payments – totaling more than $200 billion – to the settling states and territories. The MSA imposes detailed, mandatory requirements specifying how Respondents must calculate their settlement payments to the states.

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[1] Curiously, Petitioners devote a significant portion of their petition to describing and attacking a failed congressional proposal (the so-called "National Settlement") that would have settled these lawsuits a year earlier. The terms of the failed legislative proposal (including a legislative antitrust exemption that was broader than the *Noerr-Pennington* doctrine) were significantly different from the terms of the MSA. *See* Pet. at 5-8. While perhaps interesting by way of historical background, the unsuccessful legislative proposal has no bearing on the legal issues that Petitioners are asking this Court to review.

Ignoring the significant public benefits derived from the MSA, and ignoring the fact that attorneys general from more than forty states filed an amicus brief in the Court of Appeals detailing the state interests served by the MSA, Petitioners use inflammatory language to mischaracterize the MSA as a "cartel" that supposedly penalizes "renegade" cigarette manufacturers and restricts cigarette output. Their petition contains significant misstatements regarding the terms of the MSA.[2] Yet the focus of Petitioners' attack on the MSA is the mandatory settlement payments that the settling cigarette manufacturers are required to make to the states. Like any settlement agreement, the payments to the states required by the MSA increase the costs of doing business for the settling companies.

After the MSA was negotiated with the state attorneys general, it was approved by state and federal courts in all applicable jurisdictions, in conjunction with the entry of judgments dismissing the underlying State Lawsuits. The MSA was subsequently endorsed by the legislatures in these states, which enacted legislation to further the purposes of the MSA. *See* App. 39a. In sum, the MSA resulted from successful petitioning of all three branches of government – executive, judicial, and legislative. In addition, the implementation of the MSA is overseen by the state attorneys

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[2] For example, Petitioners state that the MSA sets up an "output cartel" that imposes "substantial penalties" on subsequent participating cigarette manufacturers who increase their output. Pet. at 9-10. Yet the MSA in fact contains no provisions limiting output, and the MSA payment provisions actually treat these subsequent participating manufacturers more favorably than Respondents. Similarly, Petitioners assert that the state "Escrow Statutes" force new manufacturers "into paying for the past sins of the Majors . . . ." Pet. at 11. Yet in truth, these state statutes (which, in any event, could not possibly be deemed to be acts of Respondents) simply require such manufacturers to deposit funds into escrow to satisfy *actual court judgments* against such manufacturers. App. 14a.

general, and the state and federal courts that approved the MSA retain jurisdiction over the signatories for purposes of interpreting and enforcing the terms of the MSA. Congress has also recognized the existence of the MSA and has authorized states to use MSA payments "for any expenditures determined appropriate by the State[s]." 42 U.S.C. § 1396b(d)(3)(B) (2001).

2. *Proceedings in the District Court.* Petitioners' complaint (and amended complaint) contained three antitrust counts. No constitutional claims were alleged. The first two counts alleged that Respondents violated the antitrust laws by negotiating and entering into the MSA with the states. The third count, which Petitioners dismissed voluntarily and which was not before the Court of Appeals, alleged that one of the Respondents violated the antitrust laws by acquiring three cigarette trademarks from a non-defendant company.

Respondents filed a timely motion to dismiss pursuant to Federal Rule of Civil Procedure 12(b)(6). On March 22, 2000, the District Court granted Respondents' motion to dismiss the claims challenging the MSA, and Petitioners voluntarily dismissed the remaining count.

The District Court held that because the claims were "based upon the Defendants' actions in negotiating and executing the MSA, said actions fall within the category of conduct protected by the *Noerr-Pennington* immunity doctrine . . . ." App. 75a. The District Court further held that the alleged conduct was "not subject to the 'sham' exception to the *Noerr-Pennington* immunity doctrine." *Id.* As an alternative grounds for dismissal, the District Court held that Respondents' conduct in "entering into, implementing and executing the [MSA] with the settling states . . . similarly is protected under the [*Parker v. Brown*] state action immunity doctrine." App. 77a.

3. *Proceedings in the Court of Appeals.* On June 19, 2001, the United States Court of Appeals for the Third Circuit unanimously affirmed. The Court of Appeals agreed with the District Court that "defendants are immune [from antitrust liability] under the *Noerr-Pennington* doctrine." App. 32a. On this basis, the Court of Appeals affirmed the judgment below. In *dicta*, the Court of Appeals disagreed with the District Court's alternative holding that Petitioners' antitrust claims would also be barred by the *Parker v. Brown* "state action" immunity doctrine. App. 60a. However, the *dicta* regarding the *Parker* doctrine did not affect the Court of Appeals' judgment affirming the District Court. Petitioners sought rehearing by the panel and by the Court of Appeals *en banc*. On July 24, 2001, Petitioners' requests for rehearing were denied. App. 89a-90a.

REASONS FOR DENYING THE WRIT

This petition is both substantively and procedurally baseless. First, the Court of Appeals made no new law; it simply applied the well-established *Noerr-Pennington* doctrine of antitrust immunity to the facts of this case. This Court has already denied certiorari in a case arising from the same facts, which applied *Noerr-Pennington* in the same fashion. *Hise v. Philip Morris Inc.*, 531 U.S. 959 (2000).

Second, the decision below does not conflict with any other court decision. *Every* court to date that has considered an antitrust challenge to the MSA has applied *Noerr-Pennington* in the same manner as the Court of Appeals below. The Court of Appeals' ruling that *Noerr-Pennington* may apply regardless of whether the petitioned-for government conduct meets the independent requirements for "state action" immunity is consistent with longstanding precedent. There is no need for this Court to exercise its supervisory powers in light of the uniformity of lower court decisions.

Third, because Petitioners did not allege constitutional claims in their complaint, the Court of Appeals correctly declined to consider the constitutional claims on appeal. Furthermore, the constitutional arguments are not relevant to the application of the *Noerr-Pennington* doctrine in this case.

Finally, Supreme Court review would be an inefficient use of this Court's resources because the judgment below may also be affirmed on an alternative ground, which was relied upon by the District Court – i.e., that the MSA is also entitled to immunity under the *Parker v. Brown* doctrine.

I. THERE IS NO CONFLICT: THE DECISION BELOW APPLIES *NOERR-PENNINGTON* TO THE MSA IN PRECISELY THE SAME MANNER AS EVERY OTHER COURT THAT HAS ADJUDICATED CHALLENGES TO THE MSA.

In the proceedings below, Petitioners alleged that Respondents violated the federal antitrust laws by successfully petitioning state attorneys general to enter into the MSA to resolve litigation brought by the states against them. Like every other court that has considered antitrust challenges to the MSA, both the District Court and the Court of Appeals held that defendants are immune from antitrust liability for entering into this judicially-approved litigation settlement, by virtue of the well-established *Noerr-Pennington* doctrine.

Grounded in the First Amendment, the *Noerr-Pennington* doctrine allows private parties to petition the executive, legislative, or judicial branches of government, free from antitrust liability. *E. R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 135-36 (1961); *United Mine Workers of Am. v. Pennington*, 381 U.S. 657, 669-72 (1965). In *Noerr*, this Court held that efforts to petition the government are immune from antitrust liability, regardless of any anticompetitive motivation or effect of such

petitioning efforts. *Noerr*, 365 U.S. at 138-40. This Court reaffirmed the importance of *Noerr*'s First Amendment protection a few years later:

> We conclude that it would be destructive of rights of association and of petition to hold that groups with common interests may not, without violating the antitrust laws, use the channels and procedures of state and federal agencies and courts to advocate their causes and points of view respecting resolution of their business and economic interests vis-a-vis their competitors.

Cal. Motor Transp. Co. v. Trucking Unlimited, 404 U.S. 508, 510-11 (1972). Consistent with this Court's precedents, every court that has considered whether *Noerr-Pennington* immunizes Respondents' conduct in negotiating and entering into the MSA has ruled that it does.

For example, in *Hise v. Philip Morris Inc.*, 46 F. Supp. 2d 1201 (N.D. Okla. 1999), *aff'd mem.*, 208 F.3d 226 (10th Cir. 2000), *cert. denied*, 531 U.S. 959 (2000), the district court dismissed plaintiffs' antitrust and constitutional challenges to the MSA. The court held that "defendants' activities, in negotiating the [MSA] with the several settling states and achieving a settlement agreement with those states, are protected under the *Noerr-Pennington* doctrine as conduct incidental to litigation." *Id.* at 1206. The court recognized that:

> [The *Noerr-Pennington*] doctrine would surely ring hollow if it failed to encompass private entities who, after having been sued by one or more states for similar conduct, jointly petition the states in order to achieve a mutually acceptable settlement, designed to reduce the amount of time and expense involved in defending the action.

Id. On appeal, the Tenth Circuit, relying on the "well-reasoned decision" of the district court, affirmed the district

court's decision. *Hise v. Philip Morris Inc.*, No. 99-5113, 2000 WL 192892, at *4 (10th Cir. Feb. 17, 2000).

Indeed, in the *Hise* case, one of the Petitioners herein – A.D. Bedell – filed an *amicus curiae* brief in the Tenth Circuit raising the same antitrust arguments against the MSA that it seeks to raise here. *Hise*, 2000 WL 192892, at *2 n.3. The Tenth Circuit, like the Court of Appeals below, affirmed the district court ruling that the MSA is entitled to antitrust immunity under *Noerr-Pennington*. *Id.* at *4. This Court denied certiorari in the *Hise* case on October 30, 2000.

Other courts have also applied *Noerr-Pennington* in exactly the same manner as the Court of Appeals below. In *PTI, Inc. v. Philip Morris Inc.*, 100 F. Supp. 2d 1179 (C.D. Cal. 2000), the court dismissed antitrust and constitutional challenges to the MSA brought by cigarette importers and distributors. The court held that defendants are immune under the *Noerr-Pennington* doctrine "for their activities involved with the negotiation, execution, and attempts to implement the MSA . . . ." *Id.* at 1193. The court further explained that "such conduct is precisely the type of activity the [*Noerr-Pennington*] doctrine was intended to protect." *Id.* The court in *PTI* dismissed allegations similar to those that Petitioners seek to raise here: namely, allegations that the MSA contains an illegal *per se* output restriction and that the MSA violates the Interstate Compact Clause and Commerce Clause of the Constitution. *Id.* at 1197-1203.[3]

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[3] Similarly, in *Forces Action Project LLC v. California*, No. C 99-0607 MJJ, 2000 WL 20977 (N.D. Cal. Jan. 5, 2000), *aff'd in part, rev'd in part*, No. 00-15280, 2001 WL 923124 (9th Cir. Aug. 15, 2001), the district court dismissed a constitutional challenge to the MSA. The district court observed that "defendants' action in negotiating and entering into the M.S.A. are immunized from suit under *Noerr-Pennington*." 2000 WL 20977, at *8. The Ninth Circuit affirmed this dismissal, but reversed the district court's procedural ruling that the plaintiff could not amend its complaint to add new claims. 2001 WL 923124, at *1-2. The Ninth

Like every other court that has considered whether *Noerr-Pennington* immunizes Respondents' MSA-related conduct, the Court of Appeals below concluded "that defendants engaged in petitioning activity with sovereign states and are immune under the *Noerr-Pennington* doctrine." App. 27a. The Court found "no reason to distinguish between settlement agreements and other aspects of litigation between private actors and the government which give rise to antitrust immunity." App. 31a.

In sum, no court has ever held that defendants' negotiation or execution of the MSA falls outside the scope of the *Noerr-Pennington* doctrine. The MSA was negotiated with state attorneys general, was approved by state and federal courts in conjunction with the entry of judgments implementing the settlement in each state, and has subsequently been endorsed by the legislatures of these states. Such government-petitioning conduct is not subject to antitrust liability, as the District Court, the Court of Appeals, and courts in related cases have *uniformly* held. There is no need for this Court to review this issue.

II. THE DECISION BELOW MAKES NO NEW LAW: THE COURT OF APPEALS' APPLICATION OF *NOERR-PENNINGTON* RELIES UPON AND ADHERES TO APPLICABLE PRECEDENTS FROM THIS COURT AND OTHER COURTS OF APPEALS.

The *Noerr-Pennington* doctrine unquestionably immunizes efforts to influence state governments in litigation. In *California Motor Transport*, 404 U.S. at 510-11, this Court recognized that "the right to petition extends to all depart-

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Circuit did not address *Noerr-Pennington* on appeal, as it was not the basis for the district court's denial of leave to amend. Thus, there is clearly no conflict, actual or implied, between *Forces Action* and the instant case.

ments of the Government," including the judiciary; and this Court further held that *Noerr-Pennington* applies to attempts to "use the channels and procedures of state and federal agencies and courts." Even Petitioners concede that this Court's decision in *California Motor Transport* "removes any doubt that *Noerr-Pennington* covered the conduct of litigation." Pet. at 23.

The breadth of the *Noerr-Pennington* doctrine is similarly well-established. For example, this Court has made clear that *Noerr-Pennington* applies even if there is an improper purpose or motive behind the petitioning, *see Noerr*, 365 U.S. at 138-39, even if defendants allegedly conspired with the government, *see City of Columbia v. Omni Outdoor Adver., Inc.*, 499 U.S. 365, 382-83 (1991), and even if the petitioning is "part of a broader scheme" to achieve an anticompetitive goal. *See Pennington*, 381 U.S. at 670.

Expressly relying upon this Court's decisions, the Court of Appeals properly recognized that Respondents are "immune from antitrust liability whether or not the injuries are caused by the act of petitioning or are caused by government action which results from the petitioning." App. 26a-27a. In this case, the Court of Appeals properly concluded that the *Noerr-Pennington* doctrine applied because (1) Respondents' conduct in negotiating and executing the MSA with the sovereign states is valid petitioning activity, (2) Petitioners' challenge to the legality of the MSA (and the related state "Escrow Statutes") constitutes a challenge to the government's response to petitioning conduct, and (3) *Noerr-Pennington* immunity can apply to a broader range of governmental conduct than the narrower "state action" immunity under *Parker v. Brown*.

1. The Court of Appeals, like the District Court, correctly ruled that Respondents' negotiation and execution of the MSA is protected under *Noerr-Pennington* as conduct

incidental to litigation with state governments. Because litigation activities are unquestionably entitled to *Noerr-Pennington* immunity, *see, e.g.*, *Cal. Motor Transp.*, 404 U.S. at 510-11, courts have consistently held that the decision to accept or reject an offer to settle litigation is protected under *Noerr-Pennington*. *E.g.*, *Columbia Pictures Indus., Inc. v. Prof'l Real Estate Investors, Inc.*, 944 F.2d 1525, 1528 (9th Cir. 1991) (a decision to settle litigation is entitled to *Noerr-Pennington* immunity because it "is conduct incidental to the prosecution of the suit and not a separate and distinct activity which might form the basis for antitrust liability"), *aff'd on other grounds*, 508 U.S. 49 (1993); *Campbell v. City of Chicago*, 823 F.2d 1182, 1186 (7th Cir. 1987) (settlement with local government entitled to *Noerr-Pennington* immunity); *cf. Coastal States Mktg. v. Hunt*, 694 F.2d 1358, 1367 (5th Cir. 1983) ("Given that petitioning immunity protects joint litigation, it would be absurd to hold that it does not protect those acts reasonably and normally attendant upon effective litigation.").

The MSA was negotiated with the state attorneys general and governors, it was approved by state or federal courts in each of these states, and it was endorsed by the state legislatures. The MSA thus represents both the product of Respondents' joint defense of the State Lawsuits and, once approved, the product of Respondents' petitioning of the executive, judicial, and legislative branches of government. As another court has observed, the negotiation and implementation of the MSA are "precisely the type of activity the [*Noerr-Pennington*] doctrine was intended to protect." *PTI*, 100 F. Supp. 2d at 1193.

Petitioners' contention that the decision below is implicitly inconsistent with *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*, 441 U.S. 1 (1979), is baseless. As the Court of Appeals correctly noted, *Broadcast Music* did not even address the applicability of *Noerr-Pennington*.

App. 30a. Rather, this Court ruled in *Broadcast Music* that defendants' conduct, which occurred years *after* a government decree was entered into, was not immunized by the specific terms of that decree, because the decree did not require defendants to engage in the challenged conduct. 441 U.S. at 13. The *Noerr-Pennington* doctrine was not raised, discussed, or decided by this Court in *Broadcast Music*; and as the Court of Appeals correctly noted, *Broadcast Music* is clearly inapplicable to the facts at issue here.

Similarly inapposite is the Second Circuit's decision in *PrimeTime 24 Joint Venture v. NBC, Inc.*, 219 F.3d 92, 102-03 (2d Cir. 2000). The *PrimeTime 24* case did not involve a government litigation settlement; rather, it involved copyright licensing negotiations solely involving private parties. Indeed, the Second Circuit recognized that *Noerr-Pennington* can immunize litigation settlement decisions, but ruled that the complaint before it challenged licensing negotiations that were not part of a litigation settlement. Accordingly, *PrimeTime 24* also involves a factual setting that is not relevant here.

Likewise, two other lower court cases that Petitioners cite, *Andrx Pharmaceuticals, Inc. v. Biovail Corp.*, 256 F.3d 799 (D.C. Cir. 2001), and *In re Cardizem CD Antitrust Litigation*, 105 F. Supp. 2d 618 (E.D. Mich. 2000), are not applicable to – let alone inconsistent with – this case. These two cases, like *PrimeTime 24*, involved an agreement between two *private* parties, not a litigation settlement with the *government*. *See Cardizem*, 105 F. Supp. 2d at 635 ("the Agreement settled none of the infringement claims pending in the . . . action"). Indeed, the court in *Cardizem* distinguished the facts of that case from the facts here, noting that the

Cardizem agreement was "not a result of negotiations with a state attorney general or any government official." *Id.* at 642.[4]

2. Respondents successfully petitioned the states to resolve litigation by entering into the MSA, and thus the MSA (i.e., the government's response to petitioning) clearly falls within the scope of *Noerr-Pennington* immunity. This Court has long held that *Noerr-Pennington* protects private parties from liability not only for their efforts to induce government action, but also for the acts of government in response to such petitioning. *See, e.g.*, *Noerr*, 365 U.S. at 136 (recognizing that private parties are not liable under the antitrust laws "where a restraint . . . is the result of valid governmental action"); *Pennington*, 381 U.S. at 671 ("It is clear under *Noerr* that [plaintiff] could not collect any damages under the Sherman Act for any injury which it suffered from the action of the [government]."); *see also Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 500 (1988) (*Noerr* immunity applies where injuries result from "government action"); 1 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 202c, at 159 (2d ed. 2000).

Accordingly, the District Court and Court of Appeals properly concluded that *Noerr-Pennington* protects not only the negotiation of the MSA, but also the actual implementation of the MSA once the negotiations were successful. Petitioners seek to evade *Noerr-Pennington* by characterizing Respondents' compliance with the MSA as "post-petitioning" conduct. Yet it is self-evident that since the MSA (which

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[4] Not only was the government not a party to the agreement in *Andrx*, but the government also subsequently filed suit challenging that agreement. *See Cardizem*, 105 F. Supp. 2d at 623 n.1. In contrast, the states in this case are parties to the MSA, support the legality of the MSA, and filed an *amicus curiae* brief with the Third Circuit in support of Respondents' position.

embodies the government-imposed settlement obligations) is within the scope of *Noerr-Pennington*, then compliance with the terms of the MSA is within the scope of *Noerr-Pennington* as well. Similarly, Petitioners seek to hold Respondents liable for the "Escrow Statutes" enacted by state legislatures after execution of the MSA; yet such statutes are obviously governmental conduct as well. It could scarcely be contended that private parties (like Respondents) could be held liable for a state legislature's decision to enact a statute.

In addition to this Court's precedents cited above, many lower courts have endorsed the uncontroversial principle that *Noerr-Pennington* protects private parties not only for their petitioning, but also for the "post-petitioning" effects of restraints imposed by the government. *E.g.*, *Greenwood Utils. Comm'n v. Miss. Power Co.*, 751 F.2d 1484, 1505 (5th Cir. 1985) ("First Amendment petitioning privileges would indeed be hollow if upon achieving a petitioned-for end the petitioner were then subjected to antitrust liability for his success."); *accord Sessions Tank Liners, Inc. v. Joor Mfg., Inc.*, 17 F.3d 295, 301 (9th Cir. 1994) (*Noerr-Pennington* shields defendant from liability for injuries that are the "result of governmental action").

Petitioners' reliance on *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492 (1988), is misplaced, because Petitioners here are challenging the negotiation and execution of an agreement with the government itself, not an agreement with a private litigant. In contrast, in *Allied Tube*, the plaintiff's alleged injury resulted from purely private conduct (i.e., petitioning of a *non-governmental* standard-setting organization). Thus, unlike *Allied Tube*, this suit does not raise the question of whether *Noerr-Pennington* should immunize the petitioning of private (non-governmental) entities by other private entities.

Petitioners also erroneously cite *FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411 (1990). In *Superior Court Trial Lawyers*, this Court held that private parties are not entitled to immunity when they boycott the government to coerce the government to act. That ruling is not remotely relevant here, as there is (and could be) no allegation that the states were coerced by anticompetitive conduct into settling the litigation against Respondents. *Superior Court Trial Lawyers* does not hold that government petitioners may be liable if a plaintiff is harmed directly by the petitioning conduct. To the contrary, this Court has consistently ruled that *Noerr-Pennington* immunity extends to injuries directly caused by private petitioning. *See, e.g.*, *Allied Tube*, 486 U.S. at 499 ("where, independent of any government action, the anticompetitive restraint results directly from private action, the restraint cannot form the basis for antitrust liability if it is 'incidental' to a valid effort to influence government action").

3. Petitioners' argument seems to be based on their fundamentally mistaken assumption that *Noerr-Pennington* immunity cannot apply to Respondents' conduct if *Parker v. Brown* "state action" immunity does not also apply to such conduct. This assumption is unfounded in either precedent or logic. This Court has never suggested that the *Noerr-Pennington* and *Parker* doctrines are co-extensive, or that the two doctrines must be applied in unison. To the contrary, it is well-established that *Noerr-Pennington* protects conduct that does not fall within the scope of the more limited "state action" doctrine of *Parker v. Brown*. *See, e.g.*, *Omni*, 499 U.S. at 383 (*Noerr* and *Parker* are "complementary" doctrines); *see also* 1 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 229, at 518-19 (2d ed. 2000) (recognizing that *Noerr-Pennington* immunity is "broader" than *Parker* immunity).

For example, as this Court has consistently ruled, *Parker v. Brown* protects only private conduct that is "actively

supervised" by the States, while active supervision is clearly *not* a requirement for invoking *Noerr-Pennington* immunity. *See, e.g., Omni*, 499 U.S. at 370-84. Thus, the Court of Appeals' ruling (in *dicta*) that Respondents' conduct was not sufficiently "supervised" by the States to satisfy the "active supervision" requirement under *Parker* does not remotely undercut its conclusion that *Noerr-Pennington* immunity applies to such conduct.

Petitioners' implicit assumption that petitioning conduct must be "actively supervised" to be entitled to *Noerr-Pennington* immunity is simply untenable. Because no judicial decision supports such a view, Petitioners cite rulings on the *Parker* doctrine (including portions of the decision below that analyze *Parker* rather than *Noerr-Pennington*) in a misguided effort to buttress their arguments that *Noerr-Pennington* was not properly applied in this case. Pet. at 14-16. They do not, and cannot, cite any decisions that suggest that the "active supervision" requirement is relevant to *Noerr-Pennington*.

Because there is no real conflict between the Court of Appeals' application of *Noerr-Pennington* and any other judicial interpretation of that doctrine, Petitioners ask this Court to grant certiorari in order to "brighten[] the demarcation line between *Noerr-Pennington* and *Parker*." Pet. at 19. Yet the basis upon which the Court of Appeals distinguished the applicability of these two doctrines – and the "line" between these two doctrines – has been black-letter law for more than twenty years: "active supervision" may be a requirement of *Parker* immunity, but it is not a requirement of *Noerr-Pennington* immunity. *See, e.g., Cal. Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 105 (1980); *S. Motor Carriers Rate Conference v. United States*, 471 U.S. 48, 61 (1985). The line does not need "brightening."

Petitioners' contention that there is some inchoate "inconsistency" in applying *Noerr-Pennington* but not *Parker* is also refuted by uniform case law in the lower courts. Federal courts have consistently held that *Noerr-Pennington* may apply even if *Parker* "state action" immunity does not. *See Bonollo Rubbish Removal, Inc. v. Town of Franklin*, 886 F. Supp. 955, 965 (D. Mass. 1995) (even if *Parker* did not apply, defendants "would still be shielded by the *Noerr-Pennington* doctrine") (citing *Omni*, 499 U.S. at 379-80, 383-84); *Bright v. Ogden City*, 635 F. Supp. 31, 33 (D. Utah 1986) ("Application of the *Noerr-Pennington* doctrine . . . does not depend upon a finding that the government action . . . [is] protected from antitrust liability by *Parker*."), *aff'd sub nom. Bright v. Moss Ambulance Serv., Inc.*, 824 F.2d 819 (10th Cir. 1987); *see also* 1 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 229, at 518 (2d ed. 2000) ("it seems clear that *Noerr* immunity for a private party's petition to the government in no way depends upon a finding of *Parker* immunity for the subsequent government action"). The uniform treatment of this issue by the lower courts eliminates any need for this Court to exercise its supervisory review functions.

III. PETITIONERS DID NOT ALLEGE THAT THE MSA VIOLATES THE COMMERCE CLAUSE AND THE INTERSTATE COMPACT CLAUSE, AND IN ANY EVENT, THEIR CONSTITUTIONAL ARGUMENTS ARE IRRELEVANT.

Petitioners assert that "even if settlements made with states were entitled to *Noerr-Pennington* immunity," Pet. at 5, this Court should nevertheless grant the writ of certiorari because the Court of Appeals declined to consider their claims that the MSA is unconstitutional. Yet Petitioners failed to allege constitutional claims in their complaint. Thus, as an initial matter, Petitioners' claims that the MSA is unconstitutional may be summarily disposed of, because this

Court ordinarily does not consider claims that were not properly asserted in the courts below. *See Gray v. Netherland*, 518 U.S. 152, 165 (1996) ("If the claim was not raised or addressed in federal proceedings, below, our usual practice would be to decline to review it.") (citing *Yee v. Escondido*, 503 U.S. 519, 533 (1992)); *see also Demarest v. Manspeaker*, 498 U.S. 184, 188-89 (1991) (declining to consider a question not raised in the courts below).

Moreover, Petitioners' constitutional claims are irrelevant to the *Noerr-Pennington* issue, because it is well-established that *Noerr-Pennington* applies even if petitioned-for conduct is assumed to be unconstitutional. In *Omni*, 499 U.S. at 368, 384, this Court held that *Noerr-Pennington* immunity applied to the enactment of a city ordinance even though a state court had previously invalidated the ordinance because it violated both the South Carolina and U.S. Constitutions. Similarly, in *Bates v. State Bar of Arizona*, 433 U.S. 350, 363, 384 (1977), this Court ruled that antitrust immunity under *Parker* may apply even where the government's acts are unconstitutional.

The courts of appeals are in accord. *See Greenwood Utils.*, 751 F.2d at 1499 ("In the case of petitions for legislation that ultimately turns out to be unconstitutional, *Noerr-Pennington* protection still applies."); *Subscription Television, Inc. v. S. Cal. Theatre Owners Ass'n*, 576 F.2d 230, 233 (9th Cir. 1978) (petitioning "would be considerably chilled by a rule which would require an advocate to predict whether the desired legislation would withstand a constitutional challenge").

Indeed, any contrary ruling would destroy the First Amendment underpinnings of *Noerr-Pennington*, as any advocate of government action would have to act at his peril in petitioning the government: to wit, a petitioner would become exposed to antitrust liability if the government's own

action in response to petitioning were subsequently held unconstitutional or otherwise invalid. That is clearly not the law. One of the leading antitrust authorities states flatly: "That anticompetitive legislation is subsequently held unconstitutional cannot make the legislative petitioner guilty of an antitrust violation." 1 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 206a, at 242 (2d ed. 2000). Similarly, as this Court ruled in *Omni*, a government petitioner does not forfeit his antitrust immunity even if the resulting government conduct is "substantively or even procedurally defective." 499 U.S. at 370-71.

In any event, Petitioners' constitutional attacks on the MSA are utterly baseless. Petitioners' primary argument is that the "Escrow Statutes" enacted by state legislatures are unconstitutional; yet Petitioners did not sue any states, and private Respondents obviously cannot be held liable for laws passed by state legislatures. Similarly, Petitioners argue that the MSA is an improper "compact" *among the states* that encroaches on Congress' power. Yet again, no states were sued; and as noted earlier, Congress has recognized the existence of the MSA and has expressly authorized the states to use MSA payments for all purposes "determined appropriate by the State[s]." 42 U.S.C. § 1396b(d)(3)(B) (2001).

Not surprisingly, similar constitutional challenges to the MSA have been uniformly rejected by other courts. *See, e.g.*, *Hise*, *supra*; *PTI*, *supra*; *Premium Tobacco Stores, Inc. v. Fisher*, 51 F. Supp. 2d 1099, 1102-07 (D. Colo. 1999); *Star Scientific, Inc. v. Early*, No. 3:00CV835 (E.D. Va. Mar. 26, 2001), *appeal docketed*, No. 1-1502 (4th Cir. Apr. 19, 2001); *N. Am. Trading Co. v. Nat'l Ass'n of Attorneys Gen.*, No. 01-CV-1600 (D.D.C. Sept. 18, 2001), *appeal docketed*, No. 01-7173 (D.C. Cir. Oct. 17, 2001).

In light of this uniformity among lower courts, there is no reason for this Court to reach out to address constitutional issues in a procedural context where both the Court of Appeals and the District Court properly declined to address them.

IV. THIS COURT SHOULD NOT GRANT THE WRIT BECAUSE THE JUDGMENT BELOW CAN ALSO BE DEFENDED ON AN ALTERNATIVE GROUND.

There is also an alternative ground, not included in the petition, which would independently support the Court of Appeals' judgment dismissing this action. The District Court ruled that the action should also be dismissed based on *Parker v. Brown* ("state action") immunity grounds. The Court of Appeals declined to endorse this alternative ruling due to an erroneous assumption regarding the scope of Petitioners' allegations. Indeed, when all is said and done, the core of Petitioners' argument is *not* that the Court of Appeals' application of the *Noerr-Pennington* doctrine is novel; rather, Petitioners essentially argue that the same misreading of Petitioners' allegations that led the Court of Appeals erroneously to reject *Parker* immunity in *dicta* should be used to undermine the clearly correct application of *Noerr-Pennington*. However, based on a proper reading of Petitioners' allegations, *Parker* immunity provides an alternative ground for affirming the decision below.[5]

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[5] This Court has recognized that:

> [w]ithout cross-petitioning for certiorari, a prevailing party may, of course, "defend its judgment on any ground properly raised below whether or not that ground was relied upon, rejected, or even considered by the District Court or the Court of Appeals," provided

As this Court first held in *Parker v. Brown*, 317 U.S. 341, 351 (1943), the Sherman Act does not prohibit "state action or official action directed by a state." In determining whether the *Parker* "state action" doctrine applies, this Court focuses on whether the challenged "conduct is that of the sovereign itself . . . ." *Hoover v. Ronwin*, 466 U.S. 558, 569 (1984). Specifically, this Court has recognized that where "the conduct at issue is in fact that of the state legislature or supreme court, we need not address the issues of 'clear articulation' and 'active supervision.'" *Id.*

The District Court ruled, as an alternative ground for dismissal, that Respondents' conduct in entering into the MSA was protected by *Parker* "state action" immunity. The court in *PTI*, 100 F. Supp. 2d at 1195-96, reached exactly the same conclusion in dismissing an antitrust challenge to the MSA. The Court of Appeals below rejected Respondents' *Parker* immunity argument on the grounds that Respondents might theoretically engage in post-MSA price-fixing without the "active supervision" of the States. App. 57a. Yet Petitioners did not allege any price-fixing; they challenged the MSA itself, which does not authorize price-fixing.

The MSA itself is clearly the result of "state action." Specifically, the Court of Appeals recognized that "each branch of state government had a role in the execution or operation of the [MSA]," App. 40a, that "it is evident the [MSA] was backed by clearly articulated state policy," App. 45a, and that "[t]he States here are actively involved in the maintenance" of the MSA. App. 56a. The Court of Appeals' analysis makes clear that the terms of the MSA were the

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that an affirmance on the alternative ground would neither expand nor contract the rights of either party established by the judgment below.

Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 38-39 (1989) (quoting *Washington v. Yakima Indian Nation*, 439 U.S. 463, 476 n.20 (1979)).

product of direct state involvement, and that the MSA itself falls within the scope of *Parker* immunity. App. 38a-39a. Moreover, as parties to the MSA, Respondents would also fall within the scope of *Parker* immunity. *See, e.g., Automated Salvage Transp., Inc. v. Wheelabrator Envtl. Sys., Inc.*, 155 F.3d 59, 74 (2d Cir. 1998) (a conclusion that settlement with the State was immunized under *Parker* "compels the conclusion that the [private party] defendants are shielded from antitrust liability").

The only reason the Court of Appeals rejected *Parker* immunity (in *dicta*) was that it assumed Respondents were "free to fix and raise prices" *after* the MSA was executed, and such post-MSA pricing decisions would not be "actively supervised" by the states. App. 46a. However, the Court of Appeals erred in relying on this assumption, because Petitioners never alleged that Respondents fixed prices.

In the District Court proceedings, plaintiffs categorically stated that their complaint "does not allege price fixing." Br. in Supp. of Pl.'s Mot. for Partial Summ. J. at 18 n.18; *see also* Br. for Defs.-Appellees at 24 n.9 & 36 (3d Cir.). Moreover, the Court of Appeals recognized that "the losses plaintiffs allege resulted from explicit provisions of the [MSA]." App. 17a. Petitioners "brought suit challenging sections of the [MSA] allegedly designed to maintain market share and restrict entry." App. 8a; *see* Am. Compl. ¶ 89 (challenging "the [MSA] on its face"). No provision of the MSA authorizes price-fixing, *see* App. 20a, and Petitioners made no such allegation.

In short, the Court of Appeals' *dicta* rejecting *Parker v. Brown* immunity was based on an erroneous reading of Petitioners' allegations. Once it is properly recognized that Petitioners were not alleging price-fixing, then the Court of Appeals' own legal analysis leads inexorably to the conclusion that the judgment below should be affirmed on the

alternative *Parker v. Brown* grounds, as well as on *Noerr-Pennington* grounds. Indeed, the Second Circuit has ruled that a litigation settlement agreement with a state agency is entitled to antitrust immunity under *Parker v. Brown*. *See Automated Salvage*, 155 F.3d at 67-76. The Court of Appeals did not address this case – presumably due to its mistaken belief that Petitioners were alleging price-fixing, which was not at issue in *Automated Salvage*.

As *dicta*, the Court of Appeals' analysis of *Parker* is immaterial to its judgment affirming the District Court. However, were the Court of Appeals' *Noerr-Pennington* ruling to be reviewed, an application of the *Parker* doctrine to the actual allegations in this case would provide an alternative basis for affirming the Court of Appeals.

CONCLUSION

For any and all of the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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IN THE
Supreme Court of the United States

A.D. BEDELL WHOLESALE COMPANY, INC., TRIANGLE CANDY & TOBACCO CO., on behalf of themselves and all others similarly situated,
Petitioners,

v.

PHILIP MORRIS INCORPORATED, R.J. REYNOLDS TOBACCO COMPANY, INC., BROWN AND WILLIAMSON TOBACCO CORP.,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

BRIEF AMICUS CURIAE FOR THE AMERICAN ANTITRUST INSTITUTE IN SUPPORT OF PETITIONERS

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November 21, 2001

22 pp

QUESTIONS PRESENTED

The four largest cigarette manufacturers, having a 98% share of the nationwide market, entered into a settlement agreement with 46 States to resolve lawsuits brought by the States against them. The settlement agreement contains provisions that substantially penalize any firm entering into that agreement including smaller competitors, who later signed on to the agreement for exceeding their agreed upon output. Two cigarette wholesalers brought this antitrust action on behalf of all direct buying wholesalers claiming that the output restriction is illegal *per se* under the antitrust laws. The court below held that the manufacturers' acts in furtherance of the output restrictions were immune from antitrust scrutiny under the *Noerr-Pennington* doctrine even though they did not qualify as state action under this Court's decision in *Parker v. Brown*:

1. Does the *Noerr-Pennington* doctrine immunize an output cartel controlling an entire interstate market because the provisions creating it were inserted into a settlement agreement with a group of states?

2. Does the *Noerr-Pennington* doctrine apply to an output cartel's post-petitioning anticompetitive conduct that has no antitrust immunity under state action doctrine?

3. Do the Supremacy Clause, the Commerce Clause and the Compact Clause preclude a group of States from using the *Noerr-Pennington* doctrine to immunize the operation of an interstate output cartel?

TABLE OF CONTENTS

QUESTIONS PRESENTED i

TABLE OF AUTHORITIES iii

INTEREST OF AMICUS CURIAE 1

STATEMENT OF FACTS 2

SUMMARY OF ARGUMENT 2

ARGUMENT 4

A. THE THIRD CIRCUIT'S APPLICATION OF THE *NOERR-PENNINGTON* DOCTRINE IS UNPRECEDENTED. 4

B. NON-PETITIONING CONDUCT IS NOT IMMUNIZED BY THE *NOERR-PENNINGTON* DOCTRINE. 7

C. *NOERR-PENNINGTON* "PETITIONING" DOES NOT INCLUDE POST-SETTLEMENT CONDUCT BY PRIVATE PARTIES. 8

D. PRIOR APPROVAL BY GOVERNMENT OFFICIALS DOES NOT IMMUNIZE SUBSEQUENT PRIVATE CONDUCT. 12

E. THE THIRD CIRCUIT'S DECISION CREATES UNCERTAINTY REGARDING AN IMPORTANT AND RECURRING FEDERAL QUESTION. 14

F. THERE WERE, AND ARE, LAWFUL ALTERNATIVES AVAILABLE TO THE *BEDELL* PARTIES. 15

CONCLUSION 17

TABLE OF AUTHORITIES

CASES **Page[s]**

Allied Tube & Conduit Corp. v. Indian Head, Inc., 486 U.S. 492 (1988) ..... *passim*

Andrx Pharm., Inc. v. Biovail Corp. Int'l, 2001-2 Trade Cas. (CCH) ¶ 73,363 (D.C. Cir. 2001) 11

Blackburn v. Sweeney, 53 F.3d 825 (7th Cir. 1995) 11

Broadcast Music, Inc. v. Columbia Broad. Sys., Inc., 441 U.S. 1 (1979) 12

California Motor Trans. Co. v. Trucking Unlimited, 404 U.S. 508 (1972) 8, 9

California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc., 445 U.S. 97 (1980) 7

Campbell v. City of Chicago, 823 F.2d 1182 (7th Cir. 1987) 5

Cantor v. Detroit Edison Co., 428 U.S. 579 (1976) 13

Columbia Pictures Indus., Inc. v. Professional Real Estate Investors, Inc., 944 F.2d 1525 (9th Cir. 1991), *aff'd*, 508 U.S. 49 (1993) 9

Eastern R.R. Presidents Conference v. Noerr Motor Freight, Inc., 365 U.S. 127 (1961) ..... *passim*

FTC v. Superior Court Trial Lawyers Ass'n, 493 U.S. 411 (1990) 4, 15

Forces Action Project LLC v. California, No. C 99-0607 MJJ, 2000 WL 20977 (N.D. Cal. Jan. 5, 2000), *aff'd in part, rev'd & remanded in part*, No. 00-15280, 2001 WL 923124 (9th Cir. Aug. 15, 2001) 6

Hartford Empire Co. v. United States, 323 U.S. 386, *clarified at* 324 U.S. 570 (1945) 11

Hise v. Philip Morris Inc., 46 F. Supp. 2d 1201 (N.D. Okla. 1999), *aff'd*, 208 F.3d 226 (10th Cir. 2000) 6

Otter Tail Power Co. v. United States, 410 U.S. 366 (1973) 12

PTI, Inc. v. Philip Morris Inc., 100 F. Supp. 2d 1179 (C.D. Cal. 2000) 6

Parker v. Brown, 317 U.S. 341 (1943) ..... *passim*

Premier Elec. Constr. Co. v. National Elec. Contractors Ass'n, Inc., 814 F.2d 358 (7th Cir. 1987) 11

Primetime 24 Joint Venture v. National Broad. Co., 219 F.3d 92 (2d Cir. 2000) 9

Professional Real Estate Investors, Inc. v. Columbia Pictures Indus., Inc., 508 U.S. 49 (1993) 9, 10

Sam Fox Publ'g Co. v. United States, 366 U.S. 683 (1961) 12

Silver v. New York Stock Exchange, 373 U.S. 341 (1963) 10

Ticor Title Ins. Co. v. FTC, 998 F.2d 1129 (3d Cir. 1993) 7, 13

United Mine Workers v. Pennington, 381 U.S. 657 (1965) ..... *passim*

OTHER AUTHORITIES

I Phillip Areeda & Herbert Hovenkamp, *Antitrust Law* (2d ed. 2000) 3, 10

S. Calkins, Developments in Antitrust and the First Amendment: The Disaggregation of Noerr, 57 Antitrust L.J. 327 (1988) 7

Restatement (Second) Contracts §186 11

No. 01-656

IN THE

Supreme Court of the United States

A.D. BEDELL WHOLESALE COMPANY, INC., TRIANGLE CANDY & TOBACCO CO., on behalf of themselves and all others similarly situated,

Petitioners,

v.

PHILIP MORRIS INCORPORATED, R.J. REYNOLDS TOBACCO COMPANY, INC., BROWN AND WILLIAMSON TOBACCO CORP.,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

BRIEF AMICUS CURIAE FOR THE AMERICAN ANTITRUST INSTITUTE IN SUPPORT OF PETITIONERS

INTEREST OF AMICUS CURIAE[1]

The American Antitrust Institute is an independent non-profit education, research, and advocacy organization

[1] This brief is submitted pursuant to Supreme Court Rule 37.2(a), as all parties have consented, through counsel, to its filing. Their written consent is on file with Clerk of the Court. With regard to the mandatory disclosures required by Supreme Court Rule 37.6, no counsel for any party authored this brief in whole or in part, and no person other than the American Antitrust Institute or its counsel made a monetary contribution to the preparation or submission of this brief.

concerned with the integrity of antitrust enforcement. Its Advisory Board includes leading law professors, economists, business school professors, and other experts on antitrust and competition policy. The group promotes the vigorous use of antitrust policy as a vital component of national competition policy. The organization's background and work product may be found on the Internet at www.antitrustinstitute.org.

In the instant case, the American Antitrust Institute is particularly interested in the Third Circuit's unprecedented application of the *Noerr-Pennington* doctrine. As a result of its broad consumer and cross-industry perspective, the American Antitrust Institute is uniquely placed to address the impact of this decision beyond the instant case argued by Petitioners. In particular, AAI believes the Third Circuit's decision has generated significant uncertainty regarding the application of the *Noerr-Pennington* doctrine to anticompetitive conduct contemplated in settlement agreements, conflicting with long-standing Circuit court and Supreme Court precedent. For these reasons, the American Antitrust Institute respectfully submits this brief as *amicus curiae*.

STATEMENT OF FACTS

In order to avoid unduly burdening this Court, the American Antitrust Institute adopts the statement of facts presented by the Third Circuit and by Petitioners in their petition for a writ of certiorari.

SUMMARY OF ARGUMENT

It is well-settled that the *Noerr-Pennington* doctrine immunizes private actors from antitrust liability for petitioning activities undertaken in an attempt to secure government action, even if that government action would restrain trade. *Eastern R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 135-36 (1961); *United Mine Workers v. Pennington*, 381 U.S. 657, 670 (1965). The *Noerr-Pennington* doctrine also immunizes these private

actors from antitrust liability if their petitioning succeeds and the subsequent *government* conduct does in fact restrain trade. *Pennington*, 381 U.S. at 671; I Phillip Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 202c at 159-62 (2d ed. 2000) (hereafter "Areeda"). By immunizing, *inter alia*, subsequent *private* conduct, however, the Third Circuit's opinion in *A.D. Bedell Wholesale Co., Inc. v. Philip Morris Inc.*, 263 F.3d 239 (3d Cir. 2001)(Pet. App. 1a-62a) conflicts with settled law.

As noted in the leading antitrust treatise, a "private party is not immune where the operative restraint results from its own private action inadequately supervised by the government." Areeda ¶ 229 at 519. Indeed, "courts distinguish the harm caused directly by the private parties from that caused by the government itself" because private parties petitioning the government are entitled to *Noerr-Pennington* immunity only "where government is the key deciding force." *Id.* ¶ 202c at 161, ¶ 229 at 519. In the case of successful petitioning, therefore, *Noerr-Pennington* immunity applies only to post-petitioning anticompetitive conduct that "is the result of valid government action, as opposed to private action." *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 503 (1988) (quoting *Noerr*, 365 U.S. at 136). Accordingly, while a "private party is completely immune *for seeking* [government action] . . . [the *Noerr-Pennington* doctrine] provides no shield for the private party's own subsequent market behavior," even if the private party is behaving under the auspices of prior government action resulting from its petitioning. Areeda ¶ 229 at 520-21 (emphasis in original).

In holding, *inter alia*, that the unsupervised post-settlement operation of an output cartel by private defendants is immune under the *Noerr-Pennington* doctrine, the Third Circuit's *Bedell* decision directly conflicts with well-settled law of other Circuit Courts of Appeal and this Court. In order to eliminate this conflict and related uncertainty facing litigants, this Court should grant the pending petition for a writ of certiorari with respect to the first two Questions

Presented.[2] Neither the identity of the parties agreeing to the underlying settlement nor the magnitude of their settlement should interfere with this Court applying the rule of law. *See FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411, 421-22 (1990) (even assuming that the allegedly anticompetitive conduct produced a "worthwhile" and otherwise unobtainable result, such "assumptions do not control the case, for it is not our task to pass upon the social utility or political wisdom" of the challenged conduct).

ARGUMENT

A. THE THIRD CIRCUIT'S APPLICATION OF THE NOERR-PENNINGTON DOCTRINE IS UNPRECEDENTED

The Third Circuit's unprecedented expansion of the *Noerr-Pennington* doctrine is especially stark in light of three other findings in the *Bedell* decision. First, the *Bedell* Court held that the plaintiffs properly pleaded that the tobacco manufacturers' conduct constituted an antitrust violation under the Sherman Act. Pet. App. 22a-23a. Second, the *Bedell* Court held that the anticompetitive injury at issue was proximately caused, *inter alia*, by the post-settlement conduct of the private defendants – operating the output cartel and raising prices – not merely by the signing of the settlement agreement or conduct by government officials. *Id.* at 40a-41a ("the anticompetitive injury here resulted from the tobacco companies' conduct after the implementation of the Multistate Settlement Agreement," and "we focus not on the negotiation and consummation of the Multistate Settlement Agreement, but on its actual *operation* and resulting effects, since that is the true cause of the anticompetitive effects"). Third, the *Bedell* Court held that the only other basis for immunity claimed by defendants – state action immunity under the

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[2] The American Antitrust Institute does not take any position regarding the third Question Presented.

Parker doctrine – does not apply to this anticompetitive conduct. *Id.* at 59a-60a.

The novelty of the *Bedell* holding at issue here – that post-settlement conduct by private firms is immune from antitrust challenge if previously contemplated in a settlement agreement with government officials – is belied by the Third Circuit's failure to offer any supporting authority. The closest the *Bedell* court comes to asserting that subsequent conduct by private actors is immune under the *Noerr-Pennington* jurisprudence is in its discussion of *Campbell v. City of Chicago*, 823 F.2d 1182 (7th Cir. 1987). Such reliance on the Seventh Circuit's decision in *Campbell*, however, is misplaced.

In *Campbell*, two taxicab companies agreed to settle a lawsuit they had filed against the City of Chicago "in exchange for a favorable [new] ordinance." Shortly thereafter, the taxicab companies engaged in a lobbying campaign supporting passage of the new ordinance, and the City enacted it. Alleging that this ordinance restrained trade, taxicab drivers filed an antitrust action against the City and the taxicab companies. The Seventh Circuit properly affirmed the lower court's decision that the taxicab companies' settlement and ensuing lobbying efforts were immunized from antitrust liability under the *Noerr-Pennington* doctrine. *Campbell*, 823 F.2d at 1185-87. This holding is inapplicable to the facts of *Bedell*, however, because the private post-settlement conduct at issue in *Campbell* (encouraging the City to pass the new ordinance) constituted an attempt to influence subsequent government action, and only this subsequent government action – *not* the private conduct itself – could have had anticompetitive effect.

In contrast, the private post-settlement conduct at issue in *Bedell* (operating an output cartel and raising prices) was not intended to influence government action at all, and this

private conduct itself had the direct anticompetitive effect.[3] The difference is crucial in the context of the *Noerr-Pennington* doctrine because, as noted by a leading antitrust commentator, "courts distinguish the harm caused directly by the private parties from that caused by the government itself." Areeda, ¶ 202c at 161; *see also Noerr*, 365 U.S. at 135-36 (holding there is no violation of the antitrust laws by private actors where the restraint upon trade "is the result of valid governmental action, as opposed to private action"); *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 503 (1988) (noting that absent such a distinction "competitors would be free to enter into horizontal price agreements as long as they wished to propose that price as an appropriate level for governmental ratemaking or price supports"). In light of this distinction, *Campbell* provides no support for the *Bedell* Court's holding that, *inter alia*, private post-settlement conduct is immune under the *Noerr-Pennington* doctrine.

Moreover, authority that is on point conflicts with this holding in *Bedell*. As discussed below, it is well-settled that non-petitioning conduct is not entitled to *Noerr-Pennington* immunity, that private conduct taken as a "consequence" of prior government action does not constitute petitioning, and that even the explicit approval of government officials does not immunize subsequent private conduct.

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[3] Although not cited in *Bedell*, other cases have addressed the applicability of the *Noerr-Pennington* doctrine to the Master Settlement Agreement at issue in *Bedell*. Like *Campbell*, these cases are not on point. They properly apply *Noerr-Pennington* immunity to conduct such as the negotiation of the settlement agreement, the decision to enter into it, and the subsequent passage of related state laws called for in the agreement. However, they do not address the applicability of the *Noerr-Pennington* doctrine to the private parties' post-settlement operation of an output cartel. *See PTI, Inc. v. Philip Morris Inc.*, 100 F. Supp. 2d 1179, 1193 (C.D. Cal. 2000); *Hise v. Philip Morris Inc.*, 46 F. Supp. 2d 1201, 1205-07 (N.D. Okla. 1999), *aff'd*, 208 F.3d 226 (10th Cir. 2000); *Forces Action Project LLC v. California*, No. C 99-0607 MJJ, 2000 WL 20977, at *8 (N.D. Cal. Jan. 5, 2000), *aff'd in part, rev'd & remanded in part*, No. 00-15280, 2001 WL 923124 (9th Cir. Aug. 15, 2001).

B. NON-PETITIONING CONDUCT IS NOT IMMUNIZED BY THE NOERR-PENNINGTON DOCTRINE

The *Noerr-Pennington* doctrine immunizes only conduct which constitutes "petitioning" of government officials. Non-petitioning private conduct is immune, if at all, under the *Parker* state action doctrine. *See California Retail Liquor Dealers Ass'n v. Midcal Aluminum*, Inc., 445 U.S. 97, 104 (1980) (establishing test to determine if anticompetitive private conduct qualifies as state action for purposes of *Parker* immunity). This contrast reflects the fact that while the *Parker* and *Noerr-Pennington* doctrines "are complementary expressions of the principle that the antitrust laws regulate business, not politics," they are quite distinct. Pet. App. 23a-24a (internal quotation marks omitted).

First, they have disparate doctrinal foundations, with the *Parker* doctrine based upon the states' constitutional status as at least qualified sovereigns, and the *Noerr-Pennington* doctrine based upon either the First Amendment or a statutory interpretation of the antitrust laws. *See Parker v. Brown*, 317 U.S. 341, 351 (1943) (state action immunity based upon the "dual system of government in which, under the Constitution, the states are sovereign, save only as Congress may subtract their authority"); S. Calkins, *Developments in Antitrust and the First Amendment: The Disaggregation of Noerr*, 57 Antitrust L.J. 327 (1988) (discussing the possible Constitutional/statutory bases of the *Noerr-Pennington* doctrine). Second, it follows that the jurisprudential application of these doctrines differs, as well. Although anticompetitive conduct by private parties that does not constitute "petitioning" may be immune under the *Parker* doctrine, it cannot be immune under the *Noerr-Pennington* doctrine as a matter of law. *See Ticor Title Ins. Co. v. FTC*, 998 F.2d 1129, 1138 (3d Cir. 1993) (no *Noerr-Pennington* immunity where conduct causing the anticompetitive harm was not "joint petitioning," as alleged, but "in fact nothing more than action in a private marketplace"); *Allied Tube*, 486 U.S. at 507 (the *Noerr-Pennington* doctrine does not

immunize "what are in essence commercial activities simply because they have a political impact").

In *Bedell*, the Third Circuit appropriately distinguishes between these two doctrines, implicitly recognizing that non-petitioning conduct is not immunized under the *Noerr-Pennington* doctrine. Accordingly, the *Bedell* Court's *Noerr-Pennington* analysis focuses on determining whether the private conduct in question "fits within the context of protected petitioning envisioned by the *Noerr-Pennington* doctrine." Pet. App. 27a.

C. *NOERR-PENNINGTON* "PETITIONING" DOES NOT INCLUDE POST-SETTLEMENT CONDUCT BY PRIVATE PARTIES

As already noted, "the anticompetitive injury [at issue in *Bedell*] resulted from the tobacco companies' conduct *after* implementation of the Multistate Settlement Agreement, and not from any further positive action by the states." Pet. App. 41a (emphasis added). The *Bedell* Court believed that this post-settlement conduct by private parties – including both the implementation of the cartel and the accompanying price increases – was entitled to *Noerr-Pennington* immunity as "petitioning." *See id.* at 22a, 56a-57a (plaintiffs alleged their injuries stemmed from the major tobacco companies' unsupervised operation of the cartel and decision to charge "artificially high prices"). Defining "petitioning" to include private post-settlement conduct, however, is improper.

Petitioning in the context of the *Noerr-Pennington* doctrine has been interpreted to include the use of all "channels and procedures of state and federal government" by private actors, but only in an attempt to influence prospective government decision-making or action. *California Motor Trans. Co. v. Trucking Unlimited*, 404 U.S. 508, 510-11 (1972); Areeda ¶ 229 at 519 (private parties are immune only "where government is the key deciding force"). For example, a private firm's use of the courts to file and prosecute a non-

sham[4] lawsuit against either a private or government adversary, constitutes "petitioning." *California Motor Trans. Co.*, 404 U.S. at 510-11. Likewise, conduct incidental to such litigation – including even private parties' decisions whether or not to enter into a settlement agreement – is entitled to "petitioning" immunity because otherwise the underlying litigation itself would be chilled. *See Columbia Pictures Indus., Inc. v. Professional Real Estate Investors, Inc.*, 944 F.2d 1525, 1528 (9th Cir. 1991), *aff'd*, 508 U.S. 49 (1993) ("[a] decision to accept or reject an offer of settlement is conduct incidental to the prosecution of the suit" and therefore is entitled to the same immunity, if any, of the underlying lawsuit); *see also Primetime 24 Joint Venture v. National Broad. Co.*, 219 F.3d 92, 100 (2d Cir. 2000) (enumerating other conduct incidental to such litigation that is immunized under the *Noerr-Pennington* doctrine). Direct petitioning of a government adversary in the course of litigation (*e.g.*, to accept a given settlement agreement) also is immune under the *Noerr-Pennington* doctrine. While far from an exhaustive list of "petitioning" activities, these examples share at least one common element with all private conduct entitled to *Noerr-Pennington* immunity: they are intended (either alone or in conjunction with other conduct) to influence prospective government decision-making or action, and thus can have only an indirect anticompetitive effect.

In contrast, the private post-settlement conduct at issue here is not intended to influence any prospective government decisions-making or actions, but rather is intended to have a

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[4] The limited nature of the *Noerr-Pennington* doctrine is further evidenced by the fact that not even all "petitioning" is entitled to immunity. For example, so-called "sham" or bad faith petitioning is not immune from antitrust challenge. Petitioning is characterized as a "sham" in the context of the *Noerr-Pennington* doctrine when a private actor engages in it with no objective basis for success, but instead with the intention of delaying, imposing costs upon, or otherwise harassing its competitors regardless of the outcome. *See Professional Real Estate Investors, Inc. v. Columbia Pictures Indus., Inc.*, 508 U.S. 49 (1993).

direct anticompetitive effect on the market. According to the *Bedell* court, such private conduct occurring subsequent to the successful petitioning for a settlement is entitled to *Noerr-Pennington* immunity even when it does not qualify for state action immunity under the *Parker* doctrine. Indeed, under this logic it follows that such private conduct – the operation of a cartel and the accompanying price increases – would be entitled to *Noerr-Pennington* immunity even if no settlement was reached, as long as the petitioning for a settlement took place! *See Professional Real Estate Investors, Inc. v. Columbia Pictures Indus., Inc.*, 508 U.S. 49, 57-61 (1993) (even unsuccessful petitioning can be immune under the *Noerr-Pennington* doctrine).

This attempt to broaden the definition of "petitioning" to include such post-settlement conduct by private firms is misplaced.[5] As noted by one of the leading antitrust commentators, although a private party is entitled to *Noerr-Pennington* immunity for "seeking" a specific government action, even if the government undertakes this action the "*Noerr* [*-Pennington* doctrine] provides no shield for the private party's own subsequent market behavior" permitted or even compelled by this government action. Areeda ¶ 229 at 520-21. Moreover, all "petitioning" related to a lawsuit ceases by definition once a settlement agreement is finalized: the lawsuit is no longer pending before the court, conduct incidental to the lawsuit is therefore no longer possible, and the government adversary is no longer deciding whether or not to settle.

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[5] Such a broadening also would be inconsistent with Supreme Court case law regarding interpretation of the analogous antitrust exemptions implied by certain federal statutes. Such implicit repeals of the antitrust laws are "not favored" and recognized "only if necessary to make the [statutory scheme] work, and even then only to the minimum extent necessary." *Silver v. New York Stock Exchange*, 373 U.S. 341, 357 (1963). By analogy, unprecedented expansions of the scope of common law antitrust immunities such as the *Noerr-Pennington* doctrine should be disfavored.

Thus, even if the negotiation of a settlement and the act of accepting it are immunized from antitrust liability, the settlement agreement itself may be challenged as a violation of the antitrust laws. *See, e.g., Andrx Pharm., Inc. v. Biovail Corp. Int'l*, 2001-2 Trade Cas. (CCH) ¶ 73,363, at 91,089-90 (D.C. Cir. 2001) (agreement between private litigants that was like a settlement agreement to allocate markets was not entitled to *Noerr-Pennington* immunity); *Hartford Empire Co. v. United States*, 323 U.S. 386, *clarified*, 324 U.S. 570 (1945) (settlement unlawful as part of an anticompetitive scheme). Indeed, it is well-settled that any contract, including a settlement agreement, is void to the extent it restrains trade. *See generally* RESTATEMENT (SECOND) CONTRACTS §186 ("[a] promise is unenforceable on grounds of public policy if . . . its performance would limit competition in any market").

In addition to the contract itself being unenforceable, the actual conduct contemplated in such an anticompetitive settlement agreement is also susceptible to antitrust challenge. *See, e.g., Blackburn v. Sweeney*, 53 F.3d 825 (7th Cir. 1995) (anticompetitive restraint contained in a settlement agreement unlawful under the Sherman Act). On point is *Premier Elec. Constr. Co. v. National Elec. Contractors Ass'n, Inc.*, 814 F.2d 358, 375-76 (7th Cir. 1987), in which Judge Easterbrook specifically held that the *Noerr-Pennington* doctrine does not immunize anticompetitive conduct contemplated in a settlement agreement, concluding that "[t]here is no such thing as the lawful enforcement of a private cartel."

Although the *Noerr-Pennington* doctrine provides immunity for private actors petitioning the government, once the government action that was the object of the petitioning has been taken, immunity for subsequent private conduct must be found somewhere else. Neither the *Bedell* settlement agreement itself nor private post-settlement conduct contemplated in the settlement agreement constitutes "petitioning," and therefore neither is entitled to the cloak of *Noerr-Pennington* immunity.

D. PRIOR APPROVAL BY GOVERNMENT OFFICIALS DOES NOT IMMUNIZE SUBSEQUENT PRIVATE CONDUCT

Finally, the mere fact that anticompetitive conduct undertaken by a private party was contemplated in an agreement previously entered into with government officials does not immunize that conduct from antitrust attack. As the Supreme Court held in *Otter Tail Power Co. v. United States*, 410 U.S. 366, 378-79 (1973), the fact that "provisions [restraining trade] were contained in a contract with the [federal government] is not material [to the issue of immunity because] . . . government contracting officers do not have the power to grant immunity from the Sherman Act." (Internal quotation marks omitted.) Settlement agreements are no exception:

> [A] consent judgment, even one entered at the behest of the Antitrust Division, does not immunize the defendant from liability for actions, including those contemplated by the decree, that violate the rights of nonparties.

Broadcast Music, Inc. v. Columbia Broad. Sys., Inc., 441 U.S. 1, 13 (1979).[6]

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[6] The Third Circuit's contention that *Broadcast Music* is "easily distinguished" from *Bedell* falls short. Pet. App. 30a. The fact that there was a "consent agreement" rather than a "settlement agreement" in *Broadcast Music* is a distinction without a difference, as both are contracts between private litigants and government officials in which they agree to settle the pending lawsuit. *Id.* Indeed, the *Bedell* Court itself insists that, "we are bound by holdings, not language." *Id.* (Internal quotation marks omitted.) The Third Circuit's other argument – that *Broadcast Music* is distinguishable because neither it nor a prior case it relies upon, *Sam Fox Publ'g Co. v. United States*, 366 U.S. 683, 689 (1961), cited the *Noerr-Pennington* doctrine by name – also constitutes an exaltation of form over substance, as the *Broadcast Music* language quoted above is clearly on point. Moreover, it would have been rather difficult for the Supreme Court to cite the *Noerr-Pennington* doctrine in *Sam Fox* because that case was decided four years prior to *Pennington*.

More generally, prior approval by government officials does not immunize subsequent private conduct from antitrust attack. For example, in *Cantor v. Detroit Edison Co.*, 428 U.S. 579 (1976), the Supreme Court held that neither the *Noerr-Pennington* doctrine nor the *Parker* doctrine immunized allegedly anticompetitive private conduct which had been explicitly approved by a state regulatory body and which, by law, could not even be terminated without additional state approval. The *Cantor* Court noted that the mere "authorization, approval, encouragement, or participation" by a state of "restrictive private conduct confers no antitrust immunity." *Id.* at 592-93 (footnotes omitted). Cautioning against an expansive interpretation of the *Noerr-Pennington* doctrine, the Supreme Court also pointed out that the *Noerr* opinion itself does not even address the issue of "private action taken in compliance with state law," let alone immunize such private conduct. *Id.* at 601. Similarly, the Third Circuit held in *Ticor* that the private conduct at issue – price fixing – was not entitled to *Noerr-Pennington* immunity notwithstanding the fact that several states had approved it. *Ticor*, 998 F.2d at 1138. The *Ticor* Court relied on the Supreme Court's holding in *Allied Tube* in concluding that the *Noerr-Pennington* doctrine did not apply because "Ticor's collective rate setting efforts can more aptly be characterized as commercial activity with a political impact . . . than as political activity with a commercial impact." *Id.* (citations and internal quotation marks omitted).

Because the mere imprimatur of government officials does not entitle anticompetitive conduct to *Noerr-Pennington* immunity, the fact that the *Bedell* defendants' operation of an output cartel may have been contemplated in a settlement agreement entered into with several states does not immunize that private conduct from antitrust liability. Moreover, as noted by this Court in rejecting *Noerr-Pennington* immunity despite the challenged conduct's attenuated link to government policy, "[a]lthough one could reason backwards . . . to the conclusion that the conduct at issue here is 'political,' we think that given the context and

nature of the conduct, it can more aptly be characterized as commercial." *Allied Tube*, 486 U.S. at 507.

E. THE THIRD CIRCUIT'S DECISION CREATES UNCERTAINTY REGARDING AN IMPORTANT AND RECURRING FEDERAL QUESTION

The fact that the Third Circuit's *Bedell* decision conflicts with well-settled *Noerr-Pennington* jurisprudence is particularly important because the issue here – application of the *Noerr-Pennington* doctrine to anticompetitive conduct contemplated in a settlement agreement between private defendants and state attorneys general – arises frequently. States regularly invoke their *parens patriae* authority to bring antitrust lawsuits under federal law, and subsequently enter into settlement agreements which are acceptable in the political judgment of the relevant state attorneys general. Such settlement agreements themselves, however, sometimes raise legitimate antitrust concerns from the perspective of the very third party consumers or competitors on whose behalf the relevant state attorneys general ostensibly brought the underlying lawsuits. One example recently before the Middle District of Florida is *In re Disposable Contact Lens Antitrust Litigation*, No. 1030 (M.D. Fla. Nov. 1, 2001) There, several state attorneys general and class counsel entered into a series of settlement agreements with the private defendants. At the FED. R. CIV. P. 23(e) fairness hearing, however, various third parties raised concerns regarding anticipated post-settlement conduct by one of the private defendants which consumers and competitors believe would produce an anticompetitive result. *See, e.g.*, Amicus Brief of the American Antitrust Institute with respect to the Contact Lens Settlement at 5 (July 20, 2001) ("It would be a perverse abuse of antitrust law if [defendant] were permitted to misuse a pro-competitive settlement as an anticompetitive weapon").

The applicability of the *Noerr-Pennington* doctrine to such anticompetitive conduct contemplated in a settlement agreement between private defendants and state attorneys general is not only a commonly recurring issue, it is one of

the very issues addressed by the *Bedell* court. Indeed, there was not even any need to assess the likelihood of prospective anticompetitive effect in the context of the motion to dismiss at issue in *Bedell*, as the plaintiffs alleged in their complaint that they had already suffered injury as a result of the tobacco manufacturers' anticompetitive conduct. Pet. App. 22a. ("Plaintiffs also allege the cartel injured [them] by charging artificially high prices"). As a result of the Third Circuit's immunization of, *inter alia*, such anticompetitive post-settlement conduct in contravention of well-settled *Noerr-Pennington* jurisprudence, however, private actors now face significant uncertainty regarding this important federal question. In order to eliminate this uncertainty, as well, the Court should address the doctrinal conflict created by the *Bedell* decision.

F. THERE WERE, AND ARE, LAWFUL ALTERNATIVES AVAILABLE TO THE *BEDELL* PARTIES

It is possible, of course, that a reversal of the Third Circuit's holding in *Bedell* may disrupt the settlement process currently in place regarding the states' lawsuits against the major tobacco manufacturers. Neither the identity of the parties nor the magnitude of their settlement, however, should interfere with this Court's applying the rule of law. *See FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. at 421-22 (even assuming that the allegedly anticompetitive conduct produced a "worthwhile" and otherwise unobtainable result, such "assumptions do not control the case, for it is not our task to pass upon the social utility or political wisdom" of the challenged conduct). Moreover, the *Bedell* defendants could have – and still can – moot any effects of such a legal ruling by undertaking an alternative approach to effectuate their settlement.

Indeed, the parties themselves recognized in 1997 that they could immunize their post-settlement conduct from antitrust liability by means of a congressionally-approved settlement. Pet. App. 5a-7a. It is particularly notable that the 1997 congressional proposal contained an explicit exemption

from the antitrust laws for post-settlement conduct by the tobacco manufacturers. *Id.* (the proposal also called for the major tobacco manufacturers to pay the states nearly $370 billion, or approximately 80% more than agreed to under the current settlement). Apparently both the parties and Congress itself recognized at that time that the contemplated post-settlement conduct would be actionable under the antitrust laws but for such an exemption. Although the 1997 proposal was never approved, there is nothing precluding the parties from seeking congressional approval (including an explicit antitrust exemption) again now.

An alternative to seeking a congressional settlement anew is to follow the legal road map set forth in the Third Circuit's *Bedell* opinion and take steps to satisfy the "active supervision" prong of the *Parker* doctrine, thereby qualifying for immunity under the state action doctrine. *See* Pet. App. 44a-60a. Each state can immunize the private defendants' conduct to the extent it impacts commerce in that state merely by engaging in active supervision of "the parts of the Multistate Settlement Agreement that are the source of the antitrust injury." *Id.* at 52a.[7] In fact, the Third Circuit itself suggested explicitly that "oversight or authority over the tobacco manufacturers' prices and production levels" may well suffice to satisfy this element of the *Parker* doctrine. *Id.* at 56a.

Thus, there were lawful alternatives available to immunize the *Bedell* parties' settlement at the time they entered into it. Moreover, these alternatives remain available

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[7] Of course, any attempt by states participating in the settlement to immunize the private defendants' conduct to the extent it directly impacts interstate commerce in states not participating in the settlement is susceptible to Constitutional challenge. While this issue appears to be insignificant in a case like *Bedell* where 46 states participated in the settlement and only four did not, it would be a substantial concern in a case where, for example, only two states participated in the settlement and 48 did not.

today and could keep the parties' settlement largely intact even if the Third Circuit's decision is reversed.

CONCLUSION

While the specific facts underlying *Bedell* may be unique, the *Noerr-Pennington* issues raised in the case are not. The Third Circuit decision, however, represents an unprecedented expansion of the scope of anticompetitive conduct entitled to *Noerr-Pennington* immunity. In light of this challenge to the doctrine of *stare decisis*, the Supreme Court should clarify its interpretation of the *Noerr-Pennington* doctrine by granting the pending petition for a writ of certiorari with respect to, at least, the first two Questions Presented.

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No. 01-656

IN THE

Supreme Court of the United States

A.D. BEDELL WHOLESALE COMPANY, INC., TRIANGLE CANDY & TOBACCO CO., on behalf of themselves and all others similarly situated,

Petitioners,

v.

PHILIP MORRIS INCORPORATED, R.J. REYNOLDS TOBACCO COMPANY, INC., BROWN AND WILLIAMSON TOBACCO CORP.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

REPLY BRIEF

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CORPORATE DISCLOSURE STATEMENT

Petitioners' corporate disclosure statements were set forth at page *ii* of the Petition for a Writ of Certiorari, and there are no amendments to those statements.

TABLE OF CONTENTS

	Page
Corporate Disclosure Statement	i
Table of Cited Authorities	iv
Preliminary Statement	1
The Complaint Properly Pleads An Illegal *Per Se* Output Cartel	1
The Majors' *Noerr-Pennington* Arguments Conflict With the Established Decisional Law of this Court	2
1. *City of Columbia v. Omni Outdoor Adver., Inc.*, 499 U.S. 365 (1991)	2
2. *United Mine Workers v. Pennington*, 381 U.S. 657 (1965)	3
3. *Broadcast Music, Inc. v. CBS, Inc.*, 441 U.S. 1 (1979)	3
4. *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 484 U.S. 492 (1988)	5
The Immunity For Illegal Post-Petitioning Conduct Is Governed by the State Action Immunity Doctrine	6

Contents

Page

The State Action Immunity Doctrine Does Not Authorize the Implementation Of the Nationwide Cigarette Output Cartel 7

There Was No Waiver of the Constitutional Arguments 8

Conclusion 9

TABLE OF CITED AUTHORITIES

Page

Cases:

Allied Tube & Conduit Corp. v. Indian Head, Inc., 484 U.S. 492 (1988) 5

Broadcast Music, Inc. v. CBS, Inc., 441 U.S. 1 (1979) 3, 4, 5

California Dental Ass'n v. FTC, 526 U.S. 756 (1999) 2

California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc., 445 U.S. 97 (1980) 7, 8

Campbell v. City of Chicago, 823 F.2d 1182 (7th Cir. 1987) 5

City of Columbia v. Omni Outdoor Adver., Inc., 499 U.S. 365 (1991) 2, 3

General Leaseways, Inc. v. National Truck Leasing Ass'n., 749 F.2d 586 (7th Cir. 1984) 2

Northern Securities Co. v. United States, 193 U.S. 197 (1904) 3

Parker v. Brown, 317 U.S. 341 (1943) 3, 5, 6, 7, 8

Schwegmann Brothers v. Calvert Distillers Corp., 341 U.S. 384 (1951) 3

United Mine Workers v. Pennington, 381 U.S. 657 (1965) 3

Cited Authorities

Page

United States Constitution:

First Amendment 5, 8

Petitioners hereby reply to Respondents' brief in opposition as follows.

PRELIMINARY STATEMENT

Contrary to the argument of the Majors, whether the members of a nationwide output cartel controlling virtually the entire sales of cigarettes attain antitrust immunity by setting up that cartel in a settlement agreement with a group of states, does not present some run-of-the-mill application of the *Noerr-Pennington* doctrine. The ruling below conflicts with the decisions of this Court. A definitive resolution of the issue is required not only to judicially validate or, alternatively, condemn the overcharges of billions of dollars per year from purchasers of cigarettes enabled by the cartel, but to determine whether it should serve as a valid template, in the words of the states attorneys general to conduct "meaningful settlement negotiations" with the major players in other oligopolistic markets.

The Complaint Properly Pleads An Illegal *Per Se* Output Cartel

In the courts below, the Majors sought to justify the output cartel by arguing that it was an ancillary restraint, lawful under the rule of reason. In their brief in opposition here, they now take the position that they are not operating an output cartel at all (Br. 4).[1] The complaint, however, carefully spells out how the Majors have operated the output cartel using the penalties provided in the MSA for exceeding market share allocation work to produce a drastic restriction in output (JA 59-71), and the Opinion succinctly summarizes those penalties and output restrictions. (Pet. App. at 9a-15a).

Significantly, the Majors do not contend in this Court that their engaging "in post-MSA price-fixing without the 'active supervision' of the States" would attain antitrust immunity.

1. References herein to "Br. __" are to Respondents' brief.

(Br. 22). However, according to the Majors, because the petitioners did not allege any price-fixing, they assert that $10.00/carton price rises enabled by the output restrictions in the MSA are beyond challenge. (Br. 22). As this Court explained in *California Dental Ass'n v. FTC*, 526 U.S. 756 (1999), however, it is black letter law that output restrictions are as pernicious as price fixes: "An agreement on output also equates to a price-fixing agreement." *Id.* at 777 (quoting *General Leaseways, Inc. v. National Truck Leasing Ass'n.*, 749 F.2d 586, 594 (7th Cir. 1984)).

The Majors' *Noerr-Pennington* Arguments Conflict With the Established Decisional Law of this Court

1. *City of Columbia v. Omni Outdoor Adver., Inc.*, 499 U.S. 365 (1991) ("*Omni*")

The Majors seize upon the obvious and incontrovertible proposition recognized in *Omni* that there is no conspiracy exception to the *Noerr-Pennington* doctrine,[2] to argue that they are protected under *Noerr-Pennington*, even if they "allegedly conspired with the government," citing *Omni* at 382-83 (Br. 11). This is a classic example of faulty logic. The Majors proceed to conclude from the premise that there is no conspiracy exception to *Noerr-Pennington*, that the Majors are thereby free to conspire with the States by committing acts that are not part of the petitioning process. *Omni* itself, however, refutes the very proposition urged by the Majors. In holding that the States may not "exempt a *private* action from the scope of the Sherman Act" (emphasis in original), *id.* at 379, this Court stated:

> ". . . we in no way qualify the well-established principle that 'a state does not give immunity to those

2. As pointed out in *Omni*, *id.* at 375, by definition a restraint of trade illegal *per se* under § 1 requires an agreement or, because it is illegal, a "conspiracy." Thus, a conspiracy exception to *Noerr-Pennington* would totally abolish that protection where, as usual, a § 1 charge is involved.

> who violate the Sherman Act by authorizing them to violate it, or by declaring that their action is lawful." *Parker*, 317 U.S. at 351, 63 S.Ct., at 314 (citing *Northern Securities Co. v. United States*, 193 U.S. 197, 332 (1904)). See also *Schwegmann Brothers v. Calvert Distillers Corp.*, 341 U.S. 384 (1951).

Ibid.

The issue now before this Court is whether the States, by making the settlement agreement with the Majors can authorize them to violate the Sherman Act. The opinion of the Third Circuit holds that they can, and this clearly conflicts with *Omni*.

2. *United Mine Workers v. Pennington*, 381 U.S. 657 (1965) ("*Pennington*")

In another example of twisted logic, the Majors argue that because *Pennington* held that because the protected petitioning process was "'part of a broader scheme' to achieve an anticompetitive goal" (Br. 11), therefore the operation of this cartel set up in the MSA is entitled to *Noerr-Pennington* immunity. As pointed out in the Petition (p. 15), however, *Pennington* held precisely the contrary. *Id.* at 663.

3. *Broadcast Music, Inc. v. CBS, Inc.*, 441 U.S. 1 (1979) ("*BMI*")

The Majors apparently concede that a restraint of trade embodied in a settlement agreement between private parties is not entitled to *Noerr-Pennington* immunity, but contends that such a restraint does obtain *Noerr-Pennington* immunity when made in a settlement agreement with a governmental body. (Br. 13). *BMI* flatly holds that such a restraint in a settlement with a governmental agency, there the Department of Justice, does not immunize the private parties from antitrust liability, even though the Antitrust Division had covenanted in the settlement not to attack it.

Although the Majors do not attempt to defend the primary reason advanced by the Opinion for holding *BMI* inapposite, namely, that it did not involve a settlement agreement, (Pet. App. at 30a), they advanced three other reasons why *BMI* is inapplicable (Br. 13):

a. The conduct challenged in *BMI* carrying out the restraints authorized in the agreement "occurred years *after* a government decree was entered into;" (emphasis in original)

b. The decree did not require defendants in *BMI* to engage in the challenged conduct; and

c. The concept of *Noerr-Pennington* immunity was not addressed in *BMI*.

None of these reasons withstand analysis. As to the first, the Majors do not explain why conduct engaged in "years after" the settlement agreement becomes illegal. In point of fact, under the MSA, the Majors are required to make annual settlements to the States in perpetuity or, more realistically, as long as they are able to efficiently operate the output cartel. What the decision below does is in effect to grant them a perpetual license to operate that cartel, or at least lasting for "years after" the MSA was executed.

As to the second reason, nothing in the MSA "requires" the defendants to engage in massive price increases. They do so because they are dedicated to reaping the full benefits of the cartel.

As to the third reason, namely the lack of an argument in *BMI* that *Noerr-Pennington* protection arose out of the *BMI* settlement agreement, the Majors do not argue that the parties or tribunals involved in that case were unaware that petitioning the federal government is protected under *Noerr-Pennington*. That the notion of first amendment protection for the restraint

set up in the consent decree was never discussed by anyone merely underscores its inherent irrationality.

The major difference between *BMI* and this case is that in *BMI*, unlike here, the government agency involved, the Department of Justice, did not benefit from the restraints set up in the settlement agreement.

Finally, the Majors persist in asserting that *Campbell v. City of Chicago*, 823 F.2d 1182 (7th Cir. 1987), held that post-petitioning conduct was entitled to *Noerr-Pennington* protection. As pointed out in the Petition, however (pp. 23-24), the *Noerr-Pennington* protection in that case was limited *solely* to the process of the taxicab operators' jointly petitioning the local government through litigation and lobbying legislation. The Seventh Circuit explicitly adjudicated the issue of antitrust immunity for the post-petitioning acts of the taxicab operators under *Parker v. Brown*.

In summary, the Majors can point to *no* authority of this Court which even purports to apply First Amendment petitioning protection to immunize the illegality of restraints carried out after that petitioning process was completed. There is likewise *no* authority which extends such protection to post-petitioning acts done pursuant to a settlement agreement made with a governmental body, as opposed to one made between private parties. The notion that the major firms controlling a market can with impunity operate an output cartel by virtue of its framework is being inserted in a settlement decree conflicts with the decisions of this Court discussed above and presents a clear threat to the economic freedoms guaranteed by the Sherman Act.

4. *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 484 U.S. 492 (1988) ("*Allied Tube*").

The Majors seek to distinguish *Allied Tube* by arguing that the antitrust injury inflicted in that case "resulted from purely

private conduct." (Br. 15). They then incorrectly assume that the harm petitioners sustained was caused by governmental action and thus protected under Noerr-Pennington. The Opinion, however, explicitly held that the antitrust injury sustained by petitioners resulted from private conduct. (Pet. App. at 21a-22a).

The *Noerr-Pennington* doctrine provides no immunity for anticompetitive conduct by private actors, either standing alone or with the additional participation or acquiescence of states or state officials. State participation in, approval or regulation of private anticompetitive conduct — unlike the request to engage in such conduct — is governed by the state action doctrine. Private anticompetitive conduct claimed to be protected because of state approval must be clearly articulated as state policy and closely supervised by the state. If it fails in either respect, it does not qualify as state action and is subject to antitrust scrutiny; and the fact that private actors "petitioned" a state for authority to engage in such conduct does not and cannot change this result.

The Immunity For Illegal Post-Petitioning Conduct Is Governed by the State Action Immunity Doctrine

In an effort to create a spurious issue, the Majors incorrectly assert that the petitioners make a "fundamentally mistaken assumption that *Noerr-Pennington* immunity cannot apply to Respondents' conduct if *Parker v. Brown* 'state action' immunity does not also apply to such conduct." (Br. 16). Petitioners made no such assumption. As discussed above, petitioners merely endorse the obviously correct proposition that post-petitioning conduct cannot be immunized by the constitutional protection for the *process* of petitioning. Having misstated our position in this fashion, the Majors then go on to argue that because the *Noerr-Pennington* doctrine does not require active supervision by the States, they, therefore, can carry out with impunity their illegal acts implementing the output cartel. (Br. 17-19). This illogical argument reinforces the lack of rationality of the Majors' position. Obviously, a government agency to whom the petitioning process is directed does not actively supervise that

petitioning process. What the Majors in essence are arguing is that because a group of competitors can petition a local or state governmental agency to authorize acts which are patently illegal under federal law, obtaining such authorization gives that group the right to proceed to commit post-petitioning acts not protected by state action immunity. There has never been any decision endorsing such a position.

The State Action Immunity Doctrine Does Not Authorize the Implementation Of the Nationwide Cigarette Output Cartel

The alternative ground urged by the Majors for not granting the Petition is that their conduct is clearly protected under *Parker v. Brown,* 317 U.S. 341 (1943). This position is incorrect for two reasons.

First, the Majors assume, without discussion, that *Parker v. Brown* is an *interstate* immunity doctrine. It is not. Although the Third Circuit did not address this threshold proposition, it seems reasonably self-evident that *Parker v. Brown* does not protect the operation of an *interstate* cartel. As *Parker v. Brown* itself emphasizes, *id.* at 361-62, the doctrine was formulated to protect restraints essentially authorized under local or state regulation.

Second, according to the Majors, the Third Circuit erred in holding that the Majors' post-petitioning conduct in implementing the output cartel could not qualify for state action immunity because those acts were done without any supervision by the States and hence did not meet the "active supervision" prong of *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980) ("*Midcal*"). According to the Majors, the Third Circuit reached this conclusion because it erroneously ruled that the Majors could "theoretically engage in post-MSA price-fixing without the 'active supervision' of the States." (Br. 22). The Third Circuit made no such ruling. What it did was make a careful review of the price rises that the

diligent enforcement of the output cartel enabled the Majors to make. (Pet. App. at 46a, 57a). In essence, what the Majors are arguing is that because the petitioners did not charge price-fixing, the active supervision prong of *Midcal* does not apply to their implementation of the output cartel. As explained above, once an output cartel is efficiently and thoroughly implemented, as is the case here, there is no need for the conspirators to agree among themselves to raise prices. Having choked off the supply, they are free to exploit the inelasticity of the demand. That is why output cartels, like price fixes, are illegal *per se*. The basic question before this Court is whether the Majors shall remain free to do so.

There Was No Waiver of the Constitutional Arguments

The Majors do not dispute that the petitioners argued in both courts below that the affirmative defenses of First Amendment petitioning protection and state action immunity were insufficient as a matter of law because the output cartel set up in the MSA and implemented by them violated the dormant Commerce Clause, was preempted by the Sherman Act and was a product of an unconstitutional and unauthorized interstate compact. The Majors advance no reason, plausible or otherwise, why the petitioners were obligated to anticipate the affirmative defenses of *Noerr-Pennington* and *Parker v. Brown* and set forth legal arguments in their complaint as to why these affirmative defenses, if raised, would be legally insufficient. They simply refuse to come to grips with this obvious and basically unanswerable point of rudimentary pleading.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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IN THE

Supreme Court of the United States

A.D. BEDELL WHOLESALE COMPANY, INC., TRIANGLE CANDY & TOBACCO CO., on behalf of themselves and all others similarly situated,

Petitioners,

v.

PHILIP MORRIS INCORPORATED, R.J. REYNOLDS TOBACCO COMPANY, INC., BROWN AND WILLIAMSON TOBACCO CORP.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF OF AMICI CURIAE FREEDOM HOLDINGS, INC. d/b/a NORTH AMERICAN TRADING COMPANY, INTERNATIONAL TOBACCO PARTNERS, LLC, PHILIPS & KING INTERNATIONAL, INC. and TOBACCO HOLDINGS, INC. IN SUPPORT OF PETITIONERS

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TABLE OF CONTENTS

	Page
Table of Cited Authorities	ii
Interest of Amici	1
Statement	3
Conclusion	13

TABLE OF CITED AUTHORITIES

Page

Cases:

Bacchus Imports, Ltd. v. Dias, 468 U.S. 263 (1984) 5, 12

California Retail Liquor Dealers Assn v. Midcal Aluminum, Inc., 445 U.S. 97 (1980) 12

Dennis v. Higging, 498 U.S. 439 (1991) 7

Exxon Corp. v. Eagerton, 462 U.S. 176 (1983) 5, 12

Fulton Corp. v. Faulkner, 516 U.S. 325 (1996) 5, 12

Metropolitan Life Insurance Co. v. Ward, 470 U.S. 869 (1985) 5, 12

North American Trading Company, et al. v. NAAG, et al., Civ. Act. No. 01-1600 (PLF), was filed on July 24, 2001 ..... 1, 5, 6

Northern Sec. Co. v. United States, 193 U.S. 197 (1904) 9, 12

Parker v. Brown, 317 U.S. 341 (1943) 9

Premium Tobacco Stores, Inc. v. Fisher, 51 F. Supp. 2d 1099 (D. Colo. 1999) 4

PTI, Inc. v. Philip Morris, Inc., 100 F. Supp. 2d 1179 (C.D. Cal. 2000) 4

Cited Authorities

	Page
Rice v. Norman Williams Co., 458 U.S. 654 (1982)	9, 12
Schwegmann Bros. v. Calvert Distillers Corp., 341 U.S. 384 (1951)	9, 12
South Central Bell Telephone Co. v. Alabama, 526 U.S. 160 (1999)	5, 12
Star Scientific Co. v. Earley, No. 3:00 CV 835 (E.D. Va. Mar. 26, 2001)	5
State of Dakota v. Kisanlal Bastiram Sarda, et al., S. Dak. Circuit Court, 6th Judicial Circuit, Civ. 011-218, filed 5/18/01	9
State of Idaho v. Kisanlal Bastiram Sarda, et al., Idaho District Court of the Fourth Judicial District, County of Ada, Civ. OC-0104212D, filed 7/6/01	10
State of Idaho v. P.T. Bentoel Prima, et al., Idaho District Court of the Fourth Judicial District, County of Ada, Civ. OC-0104456D, filed 7/16/01	10
State of Idaho v. P.T. Perusahaan Rokok Tjap Gudang Garam, et al., Idaho District Court of the Fourth Judicial District, County of Ada, Civ. OC-0104499D, filed 7/17/0	10
Vance v. Bradley, 440 U.S. 93 (1979)	5, 12

Cited Authorities

	Page
United States Constitution:	
Article I § 8, cl.3	1
Statutes:	
15 U.S.C. § 1	1, 9
15 U.S.C. § 26	1
18 U.S.C. § 2342	7
26 U.S.C. § 5754	4
42 U.S.C. § 1983	1, 7
36 Maine R.S. § 4383 (2001)	7
Alaska Stat. 43.50.145 (2001)	7
§§ 999.10-999.13, to Title 11 of the California Code of Regulations	11
MSA § VIII	3
MSA § IX(d)(2)(B)	6
NPM § 4383 (2001)	7
7 A.A.R. 3164, July 27, 2001	9
Other Authority:	
2001 NYSB58287	8

INTEREST OF AMICI[1]

Each of the Amici imports cigarettes (hereafter sometimes referred to as "foreign cigarettes") made by

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1. All of the parties to this proceeding have consented to the submission of this amici brief and their consents have been lodged herewith. No person or entity other than the amici curiae, or its members, has made a monetary contribution to the preparation or submission of this brief. No counsel for a party has assisted in the drafting of this brief, other than Patterson, Belknap, Webb & Tyler LLP. They acted as co-counsel with O'Connor & Hannan, LLP in representing the Amici with the exception of Tobacco Holdings, Inc. in an action against NAAG and fifteen state attorneys general charging that the state statutes declaring as contraband cigarettes made by non-complying manufacturers, including those lawfully imported to this country, and suits filed in state courts preventing the importer of such foreign cigarettes from selling them constituted an unlawful implementation of the MSA output cartel in violation of § 1 of the Sherman Act, 15 U.S.C. § 1 and discriminatory interference with their constitutional rights to engage in interstate commerce in violation of the Commerce Clause, Article I § 8, cl.3 and seeking injunctive relief to restrain such acts under § 16 of the Clayton Act, 15 U.S.C. § 26, and 42 U.S.C. § 1983. The complaint, captioned *North American Trading Company, et al. v. NAAG, et al.*, Civ. Act. No. 01-1600 (PLF), was filed on July 24, 2001 in the District of Columbia. On September 17, 2001, the district court dismissed the action for the plaintiffs' lack of standing, lack of subject matter jurisdiction and lack of *in personam* jurisdiction of the various state attorneys general even though the MSA requires them to act through NAAG and even though the district court denied discovery as to the activities of the state attorneys general within the District of Columbia. This ruling was issued from the bench and a written transcript thereof was filed on October 15, 2001. It is as yet unavailable on LEXIS or Westlaw. A notice of appeal to the U.S. Court of Appeals for the District of Columbia was filed on October 12, 2001. This action and the opinion dismissing it will sometimes be referred to herein as the *NAAG* case.

foreign manufacturers that are not members of the Master Settlement Agreement ("MSA"), described at length in the petition for certiorari. These foreign manufacturers do not make escrow funds payments under the so-called Escrow Statutes, also described in the petition for certiorari. They and the Amici were not parties, nor participated in the litigation that resulted in the MSA. They and the Amici were not parties to, nor did they participate in the MSA. Nevertheless, for the right to sell cigarettes in interstate commerce throughout the various states, the amici must pay an import duty of about 30¢ a carton in addition to the federal excise taxes which they likewise pay upon the cigarettes clearing customs. The Amici and at least 50 other importers of foreign cigarettes will effectively be wiped out unless this Court grants the petition for certiorari and bars as illegal under federal laws, the enforcement of the MSA output cartel described in the petition and in the Opinion of the Third Circuit.

The interest of the Amici thus is in the preservation of this trade and business. Because most of these importers, including the Amici, sell low priced cigarettes, the ultimate losers of this effectual prohibition of the sale of these foreign cigarettes will be the millions of smokers, who though desiring an alternative to the high priced brands manufactured and sold by the Majors, the four Original Participating Manufacturers to the MSA, will be forced to pay the higher prices imposed by the Majors. It is therefore in the interest not only of the Amici and other importers, but the country as a whole to have this Court adjudicate the legality under the antitrust laws and the United States Constitution of the output cartel set up in the MSA and implemented by the Majors and the Settling States.

STATEMENT

As stated in the Opinion of the Third Circuit ("Opinion" hereinafter):

> Together, the Renegade Clause, the Qualifying [Escrow] Statutes and the Enforcement Fund allegedly create severe obstacles to market entry, or to increasing production and market share. This is not accidental. The Multistate Settlement Agreement explicitly proclaims its purpose to reduce the ability of non-signatory cigarette manufacturers to seize market share because of the competitive advantage accruing from not contributing to the settlement.

The Enforcement Fund referred to in the Opinion is the $50 million payment made by the Majors to be used by the National Association of Attorneys General ("NAAG") set up to enforce the Escrow Statutes. MSA § VIII. This brief sets forth the anticompetitive effects upon the amici and other importers of foreign cigarettes created by the implementation of the Escrow Statutes, primarily through the Enforcement Fund.

The Amici and the other importers of foreign cigarettes have mounted a challenge, albeit a small one, to the strangulation of competitive pricing in the cigarette market accomplished by the MSA output cartel. At the time the MSA was executed on November 20, 1998, the Majors had about a 98% share of the national cigarette market. According to the Maxwell Report, dated August 21, 2001, the standard market report for the cigarette industry, due in large part to competition from foreign cigarettes, the share of the Majors

dropped in the year 2000 to 94%. This drop in market share has prompted the Settling States, the partners of the Majors in the output cartel, to take vigorous action to curtail sales of foreign cigarettes. This has consisted primarily of enforcing mechanisms set up in the MSA to protect erosion of the market share of the Majors necessary for maintaining the supra-competitive prices generated by the output cartel.

As pointed out in the certiorari petition (p.10), all of the Settling States had to and did enact so-called Escrow Statutes in order to avoid imposition of a severe diminution in settlement payments. These escrow payments require *all* cigarette manufacturers who have not joined the MSA to make non-deductible payments into escrow accounts for all of the various Settling States equivalent to the settlement payments they would have made on an annual basis if they had joined the MSA.

A principal cause of the output cartels market share erosion springs from the inherent limitation in the Escrow Statutes which require only manufacturers of cigarettes to make escrow funds payments.[2] As a matter of basic constitutional law, the obligation to make these escrow fund payments could not be imposed upon purchasers of cigarettes made by non-participating

2. The Escrow Statutes also require importers of cigarettes made in this country but shipped abroad and not intended for resale in this country, *i.e.*, gray goods, to make escrow payments. The constitutionality of requiring these re-importers of gray goods to make escrow funds payments was upheld in *Premium Tobacco Stores, Inc. v. Fisher*, 51 F. Supp. 2d 1099 (D. Colo. 1999); *PTI, Inc. v. Philip Morris, Inc.*, 100 F. Supp. 2d 1179 (C.D. Cal. 2000). These importers, however, were still free to import these cigarettes into the four Non-Settling States: Florida, Texas, Maine and Mississippi. The Majors thereafter prevailed upon Congress to enact legislation banning the importation of gray goods into this country. 26 U.S.C. § 5754.

manufacturers ("NPMs") who intended to resell them in the United States. That would have constituted preferential treatment of cigarettes offered for sale by members of the MSA and would have converted these obligations into a discriminatory excise tax because it effectively would have imposed an excise tax on all cigarettes bought from manufacturers not belonging to the MSA output cartel, and not making escrow fund payments and shipped into the Settling States. As such, it would have been invalid *per se*, under both the Equal Protection Clause[3] and under the Commerce Clause.[4] Because the Model Statute was carefully structured so as to avoid its being a discriminatory excise tax, its constitutionality was upheld in *Star Scientific Co. v. Earley*, No. 3:00 CV 835 (E.D. Va. Mar. 26, 2001).[5]

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3. *Vance v. Bradley*, 440 U.S. 93, 97 (1979); *Exxon Corp. v. Eagerton*, 462 U.S. 176, 195-96 (1983); *Metropolitan Life Insurance Co. v. Ward*, 470 U.S. 869, 882 (1985). To avoid this equal protection problem, the Model Statute was drafted the way it was, *i.e.*, not to structure the payments as *de jure* taxes but rather refundable deposits.

4. *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263 (1984); *South Central Bell Telephone Co. v. Alabama*, 526 U.S. 160, 169-170 (1999); *Fulton Corp. v. Faulkner*, 516 U.S. 325, 334-335 (1996).

5. The *Star* case is now on appeal to the Fourth Circuit, Appeal No. 01-1502. It is noteworthy for purposes of this case, however, that the *Star* decision was rendered prior to *Bedell*. The antitrust infirmities inherent in the Escrow Statute found by Bedell were never even raised by Star before the district court. Moreover, the issue of whether the Escrow Statutes *per se* constitute a direct interference with interstate commerce was not directly involved because Star itself was domiciled in Virginia and had its principal place of business there. The Amici, the plaintiffs in the *NAAG* case, did not attack the Escrow Statutes in that action but solely the unauthorized and illegal attempts by *NAAG* and the various state attorneys general to expand the reach of those Escrow Statutes to ban any sales in interstate commerce of cigarettes made by non-complying NPM's.

The MSA requires the Settling States to enforce "diligently" these Escrow Statutes. Failure to do so results in their receiving substantially less than their fully allotted share of the supra-competitive revenues generated by the output cartel. Lack of "diligent" enforcement subjects them to the so-called "NPM Adjustment" inserted in the MSA to recompense the Majors for loss of market share. MSA § IX(d)(2)(B). The failure to use "diligent" efforts to enforce the Escrow Statutes was described in a speech by Peter J. Levin, Esq., Economic Counsel for the Tobacco Project of the *NAAG*, the private association endowed with the $50 million fund by the Majors for coordinating efforts to enforce these Escrow Statutes. Mr. Levin described the following scenario in the speech given to the American Wholesale Marketers Association in which he urged these distributors, the major purchasers of cigarettes not to deal with NPMs or importers of foreign cigarettes:[6]

> So the states are going to do whatever they can to make sure that these statutes are enforced. They are very serious about it and there is a lot of money riding on it. And if there is one point that I want to make is that the states are very, very serious about this. We had an earlier seminar on statutory enforcement and one of the first power point slides that went up was a fake headline that said that State X loses hundreds of million dollars because it didn't diligently enforce its NPM Statute and that the governor was threatening to put the AG in jail and that the AG was threatening to put the NAAG people in jail.

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6. This speech is annexed as Exhibit 7 to the Dobbins Supplemental Aff., dated August 8, 2001 in the *NAAG* case.

Under this prodding, the Settling States have now proceeded to enforce "diligently" the Escrow Statutes by resorting to a number of strategies which appears to be facially unconstitutional under the Commerce Clause and thus violative of the civil rights of the Amici as well as all other importers of foreign cigarettes, and in fact all sellers in interstate commerce of cigarettes purchased from NPMs who have not made escrow fund payments, under 42 U.S.C. § 1983, *Dennis v. Higging*, 498 U.S. 439, 446, 451 (1991).

The most direct and effective way of wiping out the business of importers of foreign cigarettes is to convert the obligations to make the imposed escrow fund payments into what amounts to an excise stamp tax, mimicking the excise tax imposed by states on sales of all cigarettes but directed solely to cigarettes not made by MSA members and NPMs not making escrow payments. These states are now proceeding to do just that.

Maine and Alaska have just this past summer enacted statutes that classify cigarettes made by non-complying NPMs as contraband. 36 Maine R.S. § 4383 (2001); Alaska Stat. 43.50.145 (2001). The Maine statute subjects any wholesaler with a Maine tax stamp license to criminal excise tax punishments if it places Maine tax stamps on any cigarettes made by such an NPM § 4383 (2001). Alaska's law, effective July 3, 2001, does the same thing. It classifies as "contraband" any cigarettes made by a non-complying NPM, *i.e.*, the statute treats these in the same way as cigarettes on which a wholesaler has not placed the required excise stamp tax, and renders them subject to confiscation.[7]

7. The term "contraband" as used in connection with sales of cigarettes is a term of art, meaning packs of cigarettes on which the required state excise stamps have not been placed. 18 U.S.C. § 2342.

New York has also followed suit. It has enacted a law amending its tax law (2001 NYSB58287) which requires that all manufacturers of cigarettes sold in New York certify annually that the manufacturer is a participating manufacturer in the MSA or, if not, has made payments under the statutory schedule into the Master Escrow fund. Such certification must be delivered to the state official in order to have the appropriate cigarette stamps affixed to the cigarette package and if the certificate is not delivered or is false, any cigarette stamps affixed can be cancelled and a civil penalty of $5,000 imposed in addition to any other civil penalty.

By creating these trade barriers, Maine, Alaska and New York are apparently trying to make this cartelization of the nationwide cigarette market 100% watertight, at least in their respective jurisdictions. To do so, they necessarily have had to interfere directly with interstate and foreign commerce. If their efforts are judicially validated, it is highly probable that most of the other 43 states having these Escrow Statutes will follow their example. This high probability is apparent from the fact that *all* of the Settling States enacted Escrow Statutes to avoid having their annual settlement payments "docked", and unless they enact these contraband statutes they also risk having their annual settlement payments "docked" for lack of "diligent" enforcement.

These contraband statutes, invalid *per se* under both the Equal Protection Clause and under the dormant Commerce Clause,[8] are the final steps taken to implement the MSA output cartel.[9] They are directed at controlling all of interstate

8. See cases cited at n.3 and n.4, *supra*.

9. Arizona has even proposed a rule requiring detailed reports to be filed respecting, *inter alia*, cigarette sales by NPMs detailing (Cont'd)

commerce in cigarettes and discriminating against any cigarettes made by non-MSA cartel members that are non-complying NPMs. They are not immunized under *Parker v. Brown*, 317 U.S. 341 (1943) because they directly conflict with the prohibition in § 1 of the Serman Act, 15 U.S.C. § 1 against interstate cartels. All that the state action immunity doctrine enunciated in *Parker v. Brown*, sought to protect and all that it can protect without conflicting with the Supremacy Clause and Commerce Clause is essentially local intrastate commerce. It does not immunize actions undertaken to implement and make 100% watertight a nationwide output cartel.[10]

An alternative approach taken by the Settling States to outlaw the sales in interstate commerce of cigarettes made by non-complying NPMs is to bring actions in local state courts against any purchaser of those cigarettes that attempts to resell them in the particular Settling State. Such actions have already been instituted in South Dakota and Idaho.[11]

(Cont'd)
its sales of cigarettes in Arizona on which excise taxes are paid; the amounts of cigarettes "exported" from Arizona on which no excise taxes are paid; the failure to file such reports may result in the loss of licenses (7 A.A.R. 3164, July 27, 2001). Presumably, the next step, if the rule is adopted, is then to impose a "tax" for the benefit of the cartel upon all such cigarettes, with the penalty of not allowing sales of such cigarettes in Arizona if the tax is not paid.

10. *Northern Sec. Co. v. United States*, 193 U.S. 197, 346 (1904); *Rice v. Norman Williams Co.*, 458 U.S. 654 (1982); *Schwegmann Bros. v. Calvert Distillers Corp.*, 341 U.S. 384 (1951).

11. *State of Dakota v. Kisanlal Bastiram Sarda, et al.*, S. Dak. Circuit Court, 6th Judicial Circuit, Civ. 011-218, filed 5/18/01; (Cont'd)

These actions do not seek money damages against these sellers of cigarettes made by non-complying NPMs but rather seek solely to enjoin them from continuing to ship them into and sell them to customers located within South Dakota and Idaho. There is, of course, no basis under any principles of agency for bringing such actions in good faith. The Model Statute, Exhibit T to the MSA, which has been adopted by all of the Settling States, narrowly defines the firm obligated to make escrow payments as one which makes cigarettes.

The following hypothetical illustrates the *per se* discriminatory effects of these statutes and injunctions under the Commerce Clause: suppose that a manufacturer of dishwashers, *e.g.*, Whirlpool, has tax obligations to a particular state by reason of a franchise tax, corporate income tax, sales tax or any other state tax liability. Whirlpool sells its washers to Wholesaler X, located in another state, which in turn resells them to a retailer located the state in which the liability is owed. A statute or injunction forbidding the sale of dishwashers by third parties of any dishwashers made by a manufacturer that had not paid the tax liability, would be invalid *per se* under the Commerce Clause. The dishwasher, once sold by Whirlpool in interstate and foreign commerce, is entitled to be shipped freely by those purchasers in interstate commerce without a barrier being erected by a state based upon grievances which that state may have against the manufacturer of the article.

(Cont'd)

State of Idaho v. Kisanlal Bastiram Sarda, et al., Idaho District Court of the Fourth Judicial District, County of Ada, Civ. OC-0104212D, filed 7/6/01; *State of Idaho v. P.T. Bentoel Prima, et al.*, Idaho District Court of the Fourth Judicial District, County of Ada, Civ. OC-0104456D, filed 7/16/01; *State of Idaho v. P.T. Perusahaan Rokok Tjap Gudang Garam, et al.*, Idaho District Court of the Fourth Judicial District, County of Ada, Civ. OC-0104499D, filed 7/17/01.

What the contraband statutes and injunctions do is to convert the personal liability of the non-complying NPMs to make escrow fund payments into discriminatory excise tax obligations running with the product and, therefore, binding upon wholesales and retailers buying those products made by these manufacturers.

A different route to obtain the same result — a trade barrier against the shipment and sale of cigarettes made by non-complying NPMs — is not to seek legislative or judicial authorization for such interference, but rather simply to make a *de facto* expansion of the Escrow Statute without any enabling provision for any such regulation. Thus, the California Attorney General has proposed a regulation that effectively prohibits the sale by anyone of foreign-made cigarettes in California unless the manufacturer either belongs to the MSA or contributes to Californias escrow fund. The proposed regulation (§§ 999.10-999.13, to Title 11 of the California Code of Regulations, Chapter 11, entitled **"Confirmation of Compliance With [Escrow] Reserve Fund Requirements"**) requires that any wholesaler or distributor prior to selling cigarettes in California must receive written confirmation from a manufacturer that it has either become a participating manufacturer under the MSA or has made appropriate escrow payments. (§ 999.10) With respect to a purchase by a wholesaler from an NPM, written confirmation must be accomplished by the wholesalers obtaining a copy of the Certificate of Compliance filed by that NPM with the Attorney General that the NPM has fully satisfied its obligations under the Escrow Statute. (§ 999.11)[12]

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12. The California Attorney General held a public hearing on this proposed regulation on August 8, 2001, as a predicate to adopting it.

The Opinion has indicated that the actions taken by the Settling States in entering and carrying out the nationwide MSA output cartel are not immunized under the state action immunity doctrine for failure to meet the active supervision prong of *California Retail Liquor Dealers Assn v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980). It is also clear under established authority that the output cartel is illegal, *per se*. Therefore, all of the foregoing regulatory activity, either by statute, injunctions or executive fiat, done solely and explicitly to implement this cartel, directly contravene the prohibitions of the Sherman Act and violate the Commerce Clause and the Equal Protection Clause of the United States Constitution, as well.[13]

It is a virtual certainty that the remaining 43 Settling States, as well as the District of \Columbia and the territories which have joined the MSA will seek to enact "contraband" statutes similar to those passed by Maine, Alaska and New York. To use Mr. Levin's terms, the States are "very very serious" about enforcing the Escrow Statutes. The failure to enact contraband statutes will empower the Majors to assert that they are not "diligently" enforcing the Escrow Statutes. Alternatively, and perhaps complementing these efforts to enact such contraband statutes, the attorneys general for the Settling States will bring suits seeking to enjoin the importers from selling cigarettes made by non-complying NPMs. Obviously, as a practical economic matter, it is impossible for the Amici, as well as all other importers — small businesses, to defend a multitude of suits throughout the various Settling States.

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13. *See* cases cited in nn.3, 4 and 10, *supra*.

Unless this Court grants certiorari to review the validity of the Opinion below, it is the foregone conclusion that the importers will be in fact annihilated. This may be, as the state attorneys general and NAAG argued in the district court in the NAAG action just referred to, a good thing and constitutionally permissible. The only way that can be definitively decided is for this Court to grant the petition for certiorari to determine definitively these questions. Otherwise, the enactment of the foregoing contraband statutes, institution of multiple injunction actions and passage of regulations, such as those proposed by the California Attorney General with resultant disastrous effects on the petitioners, will inevitably occur.

CONCLUSION

The Amici submit that the questions raised by this petition are of national importance and should be decided by this Court.

Respectfully submitted,

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IN THE
Supreme Court of the United States
OCTOBER TERM, 2001

A.D. BEDELL WHOLESALE COMPANY, INC., TRIANGLE CANDY & TOBACCO CO., on behalf of themselves and all others similarly situated,
Petitioners,

-against-

PHILIP MORRIS INCORPORATED, R.J. REYNOLDS TOBACCO COMPANY, INC., BROWN AND WILLIAMSON TOBACCO CORP.,
Respondents.

ON A PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF OF AMICI CURIAE FORCES ACTION PROJECT, LLC, FREEDOM OF CHOICE, INC., CONSUMERS, LLC, SMOKERS OF THE WORLD UNITE, HAWAII SMOKERS' RIGHTS and NYC CITIZENS LOBBYING AGAINST SMOKER HARASSMENT, IN SUPPORT OF THE PETITION FOR CERTIORARI

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15pp

TABLE OF CONTENTS

Page

Table of Authorities ii

Interest of Amici and Summary Argument 1

Argument 7

1. Amici Are Adversely Affected by the MSA 7

2. The Existence of Other Litigation Justifies Resolution of Common Issues By This Court 10

TABLE OF AUTHORITIES

FEDERAL CASES **Page**

Eastern R.R. Presidents Conference v. Noerr Motor Freight, Inc. 365 U.S. 127 (1961) 3

Parker v. Brown, 317 U.S. 341 (1943) 3

United Mine Workers v. Pennington, 381 U.S. 657 (1965) 3

MISCELLANEOUS

Forbes Magazine, "The Giant Tobacco Robbery", Jan. 22, 2001 (available online at www.Forbes.com/forbes/2001 /0122/062.htmlt) 8

N.Y. Times, Nov. 21, 1998, A1, col. 5 7

N.Y. Times, Nov. 24, 1998, A20, col. 1 7

N.Y. Times, Aug. 31, 1999, C5, col. 4 8

N.Y. Times, April 18, 2001, C13, col. 4 8

N.Y. Times, April 26, 2001, C4, col. 1 8

COME NOW FORCES Action Project, LLC, Freedom of Choice, Inc., Consumers, LLC, Smokers of the World Unite, Hawaii Smokers' Rights, and NYC Citizens Lobbying Against Smoker Harassment and support Petitioners' request that this Court review and reverse the holding in *Bedell* extending application of the *Noerr-Pennington* doctrine to non-speech, post-petitioning, anti-competitive conduct and failing to properly apply the principles of *Parker* v. *Brown*, and submit the following brief in support of the petition.

Interest of Amici and Summary of Argument

Amici are grassroots organizations whose membership is composed, primarily, of cigarette consumers concerned with the preservation of adult choice to use and enjoy tobacco products, and who advocate against governmental restrictions on the behavior of citizens on matters of personal choice and lifestyle such as smoking. Amici FORCES Action Project, LLC, and Consumers, LLC, are limited liability companies organized under the laws of the State of California. Freedom of Choice, Inc., is a corporation organized under the laws of the State of Utah. Amici Smokers of the World Unite, Hawaii Smokers' Rights and NYC Citizens Lobby Against Smokers Harassment, are unincorporated voluntary membership associations. The Amici have no affiliation with, and receive no financial support from, tobacco manufacturers.

Petitioners seek review of a ruling by the Third Circuit Court of Appeals affirming the District Court's dismissal of an action filed by Petitioners. That action alleged that the Master Settlement Agreement ("MSA"), which resolved litigation by 46 states against Respondents, illegally gave monopoly pricing power in the cigarette market to Respondent Philip Morris, Inc. *et al.*, and was an explicit price-fix and output-restriction in violation of the

antitrust laws of the United States. Petitioners sought to recoup monies they have been and will be required to pay under the MSA. The explicit, almost-exclusive purpose and effect of the MSA was to allow Big Tobacco to pass through to, and to collect from, consumers the $206 billion cost of the MSA, without facing a severe price disadvantage vis á vis competitors, and to turn money over to the states. In the process, Big Tobacco could add on more and keep it for themselves, and did so.

If the Attorneys General of the 46 states who filed the actions sought to accomplish lofty goals by their suits, in the end they failed. The suits and the MSA became, solely, a vehicle for the cash-hungry states to raise billions from a very large minority of their citizens (without the due process of, *e.g.*, a duly enacted tax measure) and a vehicle for absolving Big Tobacco of the obligation to pay the huge stipulated judgments to which it consented. Indeed, the States not only relieved Big Tobacco from the liabilities they sought to impose on them by the suits, they rewarded them by, they believed, giving them monopoly pricing power. These facts cannot be ignored, passed over, and not given their due legal effect by the fact that the MSA is "one of the most significant civil settlements in the nation's history." (*FORCES Action Project, et al.* v. *State of California, et al.*, U.S.D.C., N.D. Ca. No. 3:99-CV-00607, Order Granting Motion to Dismiss and Denying Leave To File Second Amended Complaint, 1/5/00, PACER Dckt. No. 81.) That fact simply illustrates the enormity of the wrong done by the States and Big Tobacco to their customers, citizens and taxpayers.

While Petitioners are the direct purchasers of the products of Respondents Philip Morris, Inc., *et al.*, the price increases were passed on to Amici, the indirect, but ultimate purchasers of Respondents' products. As consumers, Amici's members are the primary beneficiaries of

the antitrust laws of the United States. No persons, including Petitioners and Respondents, were more deeply and centrally affected by the MSA than were Amici.

In addition to their economic interests, Amici, as consumers and citizens, have a keen desire to restore the important consumer-protection principles of *Parker* v. *Brown*[1] that the Third Circuit removed in the present case. While the Third Circuit in *Bedell* clearly, and correctly, held, that the parties to the MSA had not secured *Parker* immunity for the price-fix and output restriction mandated by the MSA, it held, nonetheless, that the MSA, and the price increases mandated and carried out pursuant to it, were immune under the *Noerr-Pennington* doctrine.[2] Prior to *Bedell*, application of *Noerr-Pennington* had been restricted to concerted speech ("petitioning") that sought exemptions from the antitrust laws for contemplated, substantive anticompetitive conduct. *Noerr-Pennington* held that Free Speech principles trumped antitrust principles and that such speech was protected. Prior to *Bedell*, only one court had held that the free-speech principles enunciated in *Noerr* and *Pennington* could immunize substantive anticompetitive activity that constituted a *per se* violation of the Sherman Act. From a time-line perspective, *Noerr-Pennington* (on appropriate facts) gave immunity for joint anticompetitive conduct leading up to governmental action, but whether immunity was achieved for the substantive activity thereafter was determined by *Parker* v. *Brown* principles.

The Third Circuit displaced *Parker* v. *Brown*

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[1] 317 U.S. 341 (1943).

[2] *Eastern R.R. Presidents Conference* v. *Noerr Motor Freight, Inc.*, 365 U.S. 127 (1961); *United Mine Workers* v. *Pennington*, 381 U.S. 657 (1965).

as the law governing post-settlement activities and replaced it with *Noerr-Pennington*. The Third Circuit failed to understand the relationship between *Noerr-Pennington* and *Parker* and extended *Noerr-Pennington* to activity that does not invoke First Amendment considerations. Nothing in the prior opinions of this Court suggests such a result and such a result flies in the face of the reasoning of this Court in *Noerr, Pennington, Parker* and their progeny.

Parker v. *Brown* ensures that where the States propose to remove competition as the dominant force in pricing goods and services, that decision shall be made only by the State, acting as the sovereign representative of all of its citizens, and not by individual public officials acting without explicit, *pre-existing* mandate from the State. *Parker* also ensures that when the States, acting in a sovereign capacity, determine to allow a monopoly or oligopoly, they shall closely regulate and supervise pricing by the monopoly or oligopoly. While the Third Circuit recognized *Parker* principles and correctly applied them in *Bedell* (holding that Respondents had not secured *Parker* immunity) it also found them largely irrelevant when it, nonetheless, extended *Noerr-Penningon* into post-settlement activity.

If post-settlement, non-speech activity is at issue, there are no predicate facts to invoke First Amendment and *Noerr-Pennington* principles. And if *Noerr-Pennington* is applied to post-settlement, non-speech activity, *Parker* v. *Brown* is robbed of any meaning and consumer protection has been eroded very significantly. The Attorneys General will have succeeded in gaining authority for activities previously within the sole province of the legislature and regulatory agencies. Unlike the legislature and the regulatory agencies, the Attorneys General are not suited, let alone authorized, to perform the close supervision and regulation that a grant of monopoly pricing power requires.

Some of the Amici are plaintiffs in an action

pending in the United States District Court for the Northern District of California (*FORCES Action Project, supra*). In August, 2001, the United States Circuit Court of Appeals for the Ninth Circuit reversed an order of the District Court denying Amici leave to amend their complaint to state a claim under the antitrust laws for injunctive relief. Amici have now renewed their motion for leave to file a Second Amended Complaint. A ruling by this Court on the validity of the ruling by the Third Circuit will impact Amici's pending case, and others pending in other courts throughout the country.

Finally, Amici suggest that the absence in the MSA of any provisions regarding, either, the manner and amount of the price increases mandated by the MSA, or any restrictions on the uses of the monies paid by tobacco consumers to the States (through Respondents), has resulted in having tobacco consumers bear an unconscionably disproportionate share of the costs of general public improvements, benefits and expenditures which are financed by the $206 billion tobacco consumers will pay. Tobacco consumers did not participate in the negotiations over the MSA directly nor were they represented indirectly by the States acting as sovereign. The monies which the MSA mandated be paid by consumers are being used to pay for a broad array of general public benefits, improvements and expenditures and are, truly, the extraction of a tax without representation.

In summary, Amici and the millions of tobacco-consuming members of the public whose interests they seek to protect have a tangible, profound interest in the antitrust and constitutional questions presented by the Petition. As the petition shows, the output restrictions embodied in the MSA's so-called Renegade Clause (MSA § IX(i)) have enabled the major cigarette manufacturers (the "Majors") to boost cigarette prices far beyond levels needed

to fund the settlement payments to the States. The supracompetitive price increases already have cost tobacco consumers billions of dollars and the resulting revenues to the States pay for matters of general public benefit whose costs should be shared by all.

Argument

Amici's arguments, summarized above, that the MSA and the conduct carried out pursuant to it were illegal, and the argument that the Third Circuit misapplied *Noerr-Pennington*, are fully supported and discussed in the brief of Petitioners and other amicus briefs filed herein. Those arguments are not repeated here, but are incorporated by reference. Amici present supplemental facts and argument regarding the economic impact upon them of the illegal price-fix and output restriction and regarding other litigation that attacks the MSA, both of which justify review by this Court.

1. Amici Are Adversely Affected by the MSA

The final agreement between the 46 States Attorneys General and the Majors was publicly announced on Friday, November 20, 1998. N.Y. Times, Nov. 21, 1998, A1, col. 5. Industry analysts at that time computed that the costs of the $206 billion settlement, to be paid to the States over 25 years, likely would be passed on to tobacco consumers by means of price hikes totaling 35 to 40 cents a pack. *Id.*

It took only until the following Monday to discover how far off the mark the analysts were, and how blind they were to the supracompetitive pricing scheme put into place by the MSA's output restrictions. On November 23, 1998 — the same day the Majors executed the MSA — Philip Morris and RJR within minutes of each other announced a price increase of 45 cents a pack, which was quickly matched by Lorillard and Brown &Williamson. N.Y. Times, Nov. 24, 1998, A20, col. 1. Thus, by the time the sun went down on the first day of the MSA's legal existence, the Majors already were positioned to begin extracting supracompetitive profits from tobacco consumers.

But this was only the beginning. The Majors raised prices by another 18 cents a pack in August 1999, by

13 cents a pack in January 2000, by 6 cents a pack in July 2000, by 14 cents a pack in December 2000, and by 14 cents a pack in April 2001. The wholesale price of a carton of cigarettes has increased from approximately $19.00 to about $30.00 in less than three years, or more than 60 percent. Petition at 12-13; Joint App. at 680; N.Y. Times, Aug. 31, 1999, C5, col. 4, April 18, 2001, C13, col. 4 & April 26, 2001, C4, col. 1.

The impact of the supracompetitive pricing on tobacco consumers can be measured by comparing the additional revenues generated by these phenomenal price increases and the payments made by the Majors under the MSA. Through April 2001, the net annual payments to the settling States under the MSA totaled approximately $16 billion. In this same period the several price increases generated additional revenues of approximately $29 billion (after 9 percent downward adjustments for normal free market price rises and for market share loss), or almost double what was needed to fund the MSA payments. Little wonder that Philip Morris, the dominant company with over 60% of the premium and 50% of the total market, in its SEC filing for the second quarter 2001 reported record profits for its domestic cigarette company. *See also* Forbes Magazine, "The Giant Tobacco Robbery", Jan. 22, 2001 (available online at www.forbes.com/forbes/2001/0122/062.htmlt); Pet. App. at 14a-16a.

The MSA gives the revenue-hungry States a vested interest in the Majors' maintenance of market share and excessive profits. So long as the Majors are protected against market share erosion, starting in April 2002 the payments to the States for that year and annually thereafter will go from $8 billion eventually peaking at $9 billion. However, as recently reported by the Associated Press on October 21, 2001, "[t]he National Conference of State

Legislatures released a report in August [2001] showing that only 5 percent of the tobacco settlement money was being used on smoking prevention. Some states used the settlement money to make up shortfalls in state budgets and fund programs that had nothing to do with smoking." For example, Tennessee spent $560 million of its MSA money — four years' worth — to balance its current budget. Other states already committed to using hundreds of millions of MSA dollars to balance their budgets include Michigan, Wisconsin, Missouri, Montana and Ohio.

Effectively, this constitutes taxation of tobacco consumers without representation. Smokers were absolutely excluded from participating in the underlying litigation and negotiation of the MSA. In California, for example, the Attorney General of that State successfully opposed an intervention petition by one of the present Amici, to intervene in the action it had filed against Respondents so that consumers would have a voice in and be represented at those proceedings. While the Attorneys General have argued that they brought the underlying actions in the public interest and, thus, that smokers' interests were represented, the public was and is widely divided on tobacco issues and no attorney could adequately represent both sides on tobacco issues. To the extent that the Attorneys General did, in fact represent smokers, they breached their duty to them when they agreed to allow the tobacco companies to shift the costs of the settlement to them (and were unsuccessful in securing *Parker v. Brown* and *Noerr* immunities either for themselves or the tobacco companies).

2. The Existence of Other Litigation Justifies Resolution of Common Issues By This Court

As noted above, some of the Amici are plaintiffs in the above-mentioned *FORCES Action Project* litigation against Respondents and the States (who were not defendants in *Bedell*) in an action alleging that the MSA, and the conduct carried out pursuant to it, are illegal anticompetitive activities. The [Proposed] Second Amended Complaint filed by Amici in that case does not merely complain of the MSA, but, rather, places it in the context of and capstone of a long-standing illegal conspiracy by the Majors to control cigarette pricing. Amici allege that, in entering into the MSA, the States joined the conspiracy and gave the Majors the long-sought monopoly pricing power.

The allegations of the long-standing conspiracy set forth in Amici's pending case also closely track the allegations of the Second Consolidated Amended Class Action Complaint in *In Re Cigarette Antitrust Litigation*, MDL No. 1342, U.S.D.C. N.D. Ga. No. 1:00-cv-447 JOF. While that complaint focuses on the pre-MSA conduct of Respondents, it recites the price increases adopted after the MSA as evidence of the conspiracy and as further acts carried out pursuant to the conspiracy.

In addition to *In Re Cigarette Antitrust Litigation* the MSA was attacked in *PTI, Inc.* v. *Philip Morris, Inc., et al.*, 100 F. Supp. 2d 1179 (2000), and in a pending action in the Western District of Pennsylvania, *Mariana v. Fisher*, Civil Action No. 1:01-CV-2070 (SHR). An additional antitrust challenge to the MSA is pending on appeal from an order of dismissal in a case filed in the District of Columbia by cigarette importers, *North American Trading Co. v. National Association of Attorneys General*, Civil Action No. 01-1600 (PLF). Amici are generally aware

that the MSA has been and is under attack by a variety of public-health interests and competitors in a large number of cases, although Amici do not have information to specifically identify them.

Litigation will continue on a broad scale in the District Courts and Courts of Appeal. The sheer number of cases, as well as the importance of the issues, fully recommend review by this Court at this time to resolve core issues presented in all.

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Respectfully submitted,

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